# Forestry Innovation Investment Ltd.

## 2005/06 Annual Service Plan Report

**Statistics and other figures in this report were sourced from:**

The Coalition of Forest Industries
International Wood Markets
BC Stats
Stats Canada
BC Competition Council
Forest Products Association of Canada
Decima Research

**Library and Archives Canada Cataloguing in Publication Data**

British Columbia. Forestry Innovation Investment
Annual service plan report. - 2005/06-

Annual.
Continues: British Columbia. Forestry Innovation Investment. Annual report.
ISSN 1715-3808 = Annual service plan report (British Columbia. Forestry Innovation Investment)

1. British Columbia. Forestry Innovation Investment - Periodicals.
2. Forest products - British Columbia - Marketing - Periodicals.
3. Forest products industry - Economic aspects - British Columbia - Periodicals.
4. Forest products industry - Government policy - British Columbia - Periodicals.
I. Title.
II. Title: Forestry Innovation Investment Ltd. annual service plan report.

HD9764.C2C3 354.5'1097105 C2005-960343-4

Forestry Innovation Investment Ltd.

Decima Research provided opinion research quoted in this report.
R.E. Taylor & Associates Ltd. provided market, sales and other research used in this report.
Ipsos Reid Public Affairs provided statistical data for this report.

| | |
|---|---|
| Message from the Chair to the Minister of Forests and Range | 2 |
| Message from the Chief Executive Officer | 3 |
| Corporate Overview | 5 |
| Key stakeholders and partners | 5 |
| Core program areas and services | 5 |
| Strategic Context | 9 |
| Corporate Governance | 9 |
| Governance Principles | 10 |
| Report on Performance | 11 |
| Alignment with government's strategic plan | 22 |
| Goals and achievements at a glance | 24 |
| Management discussion and analysis | 30 |
| Financial Statements | 34 |
| Service Plan Goal Changes Summary | 43 |
| Glossary | 45 |
| Contact us | Back Cover |

06 June, 2006

The Honourable Rich Coleman
Minister of Forests and Range
Province of British Columbia

Dear Minister:

When Forestry Innovation Investment Ltd. was formally established in 2003, it was charged with supporting industry efforts to innovate, to maintain and grow market share for BC's first-class forest products.

Never before has the mandate and work been so important.

The United States was a robust marketplace for BC suppliers in 2005/06 as natural disasters and record-setting new-home construction created a strong demand for structural lumber and panel products. Between 1993 and 2003, the value of international trade in wood and forest products grew by 50% to over US$150 billion annually. Growth continues at an estimated rate of 5% per year.

As a result of this growth, British Columbia's forest products are facing increased competition from countries such as China, Russia, the European Union and the Southern hemisphere; markets have become more fragmented, competitive and price-sensitive.

A rapidly rising Canadian dollar, soaring energy prices, increasing transportation costs and aggressive pricing by foreign competitors compounds the situation.

In partnership with FII, the BC industry maintains strong forest product marketing, sales and sustainable forest-management messaging. Assurances that BC's wood comes from well-managed forests is an increasingly valuable asset as concerns about illegal harvesting, over harvesting and other issues rise elsewhere in the world.

In 2005/06, FII achieved performance targets across all goals and objectives – from dismantling trade barriers in Japan, Korea and China to launching an ambitious mountain pine beetle program and strengthening BC's sustainable forest management message through market meetings, tradeshows and information sharing.

FII stakeholders endorsed the work of FII and its staff through a detailed stakeholder survey. Over 40 key industry representatives from forest companies, associations and the sector, government officials, embassy staff and others contributed their views to the survey. The preponderance of opinions was very favourable.

This reflects the quality of the staff in the organization and bodes well for the future where continued excellence and greater innovation and collaboration will be required.

The 2005/06 Forestry Innovation Investment Ltd. annual report was prepared under my direction in accordance with the Budget Transparency and Accountability Act. I am accountable for the contents of the report including the selection of performance measures and how the results have been reported. The information presented reflects the actual performance of Forestry Innovation Investment Ltd. for the 12 months ended March 31, 2006.

All of the significant decisions, events and identified risks as of June 06, 2006, have been considered in preparing the report.

The information is prepared in accordance with the BC Reporting Principles and represents a comprehensive picture of our actual performance in relation to our service plan. The measures presented are consistent with Forestry Innovation Investment Ltd.'s mission, goals and objectives and focus on aspects critical to the organization's performance.

I am responsible for ensuring internal controls are in place to ensure performance information is measured accurately and in a timely fashion.

This report contains estimates and interpretive information that represents the best judgment of management. Any significant limitations in the reliability of data are identified in the report.

Doug Konkin
Board Chair

2005 and early 2006 marked a period of significant evolution in world wood markets.

Fuelled by continuing low interest rates and a growing supply of affordable new homes for eager buyers, the United States counted a record 2,000,000 new-home starts in 2005, helping it to remain the number one and most successful market for BC forest products.

Elsewhere, the past year saw China's continued emergence as one of the world's leading wood products manufacturers and a growing supplier of finished products. Conversely, it was an increasingly promising market for BC exporters with more than 328,000 cubic metres of softwood lumber flowing into China in 2005, a 274 per cent increase in shipments in just five years.

With the rapidly evolving role of China in world markets and the success of FII's Dream Home Canada demonstration project, FII and its industry partners continue to refine their market activities in China.

By combining forces under the Canada Wood Group umbrella, the industry is focusing on training, technology transfer and quality assurance initiatives as well as demonstration of renovation and building-upgrade projects to better position BC wood products to maximize market gains.

In Japan, the housing market is on the upswing as consumers see the design flexibility of wood-frame construction and benefit from updated building codes that allow larger structures. BC producers have renewed opportunities to provide increasingly busy builders there with top-quality dimension and BC finishing products.

Furthermore, Japanese homeowners are increasingly concerned about the environmental properties of the products they buy and that plays into BC's strength as a leading supplier of products from sustainably managed forests.

In Indonesia, last fall FII sponsored the placement of 10 prototype homes in a village near Banda Aceh to support rebuilding following the Dec. 26, 2004 tsunami. The houses were supplied by four BC firms that specialize in pre-cut homes and provide a demonstration of the versatility, flexibility and safety of wood in the face of recurring earthquakes.

Through this initiative, FII is hopeful BC firms will create new relationships with customers in Indonesia and other regions where low-cost housing is a priority.

Domestically in 2005/06, the Government of Canada partnered with the Province of BC to launch the $100 million Mountain Pine Beetle Emergency Response: Canada-BC Implementation Strategy.

As the beetle marches across much of central BC and threatens to kill 80% of the Interior pine trees by 2014, FII is supporting the development of new products, uses and market understanding about the affected wood's integrity and durability.

In 2005, FII established a mountain pine beetle program, hired a director to lead the initiative and distributed over $1 million for 15 projects to support product innovation and research into expanded use of this structurally sound wood.

As competitors ratchet up the stakes in international markets, the sales landscape for wood continues to demand responsiveness and adjustment. While BC producers enjoy the good returns from the booming US market, the industry must remain attentive to the inroads being made by suppliers from other jurisdictions and pursue diversification in new and emerging markets.

As we move through 2006/07, FII remains committed to innovative programming and services that bolster partnerships that give strength to BC's market presence and reputation as a world-class supplier of top-quality forest products from sustainably managed forests.

In the year ahead we will continue to draw on the strength of FII's staff, the synergies of our partnerships, our increasing investments and the inherent desirability of BC products to ensure that BC remains an international force in the marketplace.

K. Baker

Ken Baker
CEO

certified

jurisdiction

The British Columbia government owns approximately 95 percent of the province's land base. The forest industry that operates on some of that land is a $14 billion industry that touches every corner of the province and directly employs an estimated 90,000 residents within it. Including secondary employment of about 130,000 workers, BC's forest sector is a major BC employer.

The prosperity of the BC forest industry is dependent on continuing demand for our products in world markets. Approximately 83% of our forest products are sold to customers in the United States and Japan. The prosperity of our forest sector, and our province, depends on maintaining and building demand for our products in these and other world markets, markets that are becoming increasingly complex and competitive.

Forestry Innovation Investment Ltd. (FII) was established in March, 2003, with a mandate to:

- help maintain, build and diversify market opportunities for BC's forest products;
- help break down trade and market barriers to ensure opportunities for BC wood;
- work with the forest industry to position BC as a global leader in sustainable forest management; and,
- help ensure the forest sector, through strong international sales, continues to be a leading contributor to the BC economy.

FII delivers on its goals through formal arrangements with industry associations, academic institutions and other organizations, engaging external consultants and its own expertise.

FII supports the forest sector by:

- undertaking market research and supporting the development of collaborative market-development strategies;
- sponsoring demonstration projects and technology transfer;
- working with foreign governments to develop their codes and standards to recognize BC species and their quality;
- testing the attributes of new forest products;
- promoting BC's wood products and available species; and,
- communicating BC's forest-management record.

FII is particularly committed to long-term engagement in markets that require significant investment of time to mature the relationship.

The FII model also lends itself to a strong federal/provincial/private collaboration with:

- a critical mass of expertise and energy;
- common branding in foreign markets;
- collaborative funding opportunities; and,
- efficient harmonization of roles and responsibilities.

FII works with its partners, forest industry associations, education and research institutions, other government departments and others to:

- identify opportunities and challenges that require follow-up, study or action;
- provide funding to industry associations and institutions to research specific markets and develop innovative products that will open doors to new wood sales or help retain or expand sales in existing markets;
- develop innovative marketing initiatives to promote and position BC wood products and species;
- demonstrate wood-frame construction products and techniques in the emerging Chinese market;
- play a key role in the Mountain Pine Beetle Emergency Response: Canada-BC Implementation Strategy – the province's three-year business plan for the $100 million received from the federal government to mitigate impacts of the beetle;
- provide factual information on BC's forest management practices to international buyers; and,
- challenge legislation in other jurisdictions that might discriminate against the flow of BC wood.

### Key stakeholders and partners

FII's key stakeholders and partners include:

- BC's forest companies;
- the forest industry trade associations that represent large and small companies around the province;
- federal government departments such as Natural Resources Canada (Canada Wood Export Program) and Canada's international consulates and embassies;
- academic and research institutions engaged in forest product studies; and,
- the Ministries of Forests and Range, and Economic Development.

## CORE PROGRAM AREAS AND SERVICES

FII categorizes its activities according to the following three business areas:

- Market Development Programs;
- The BC Market Outreach Network Program; and,
- Corporate support.

During the third quarter of 2005/06, the FII undertook an assessment of International Marketing and Product Development (IMPD) activities with a view to focus them more effectively. As a result of that process, FII consolidated the IMPD activities into one Market Development Business Area to address all relevant activities, whether market access, product development, or promotional in nature.

Over 95% per cent of the Market Development Business Area (MDBA) budget is invested in projects, research and marketing programs.

The MDBA supports the BC forest sector through six programs:

**International Marketing** – BC is the world's largest exporter of softwood lumber so maintaining and growing international markets is key to the future prosperity of the provincial forest sector. International marketing activities focus on researching foreign markets and funding marketing campaigns at the individual market level.

Market research provides insights into BC's competitive position globally, especially opportunities in the emerging markets of southeast Asia, and market intelligence on the activities of foreign competitors.

Marketing campaigns are supported by funding the activities of BC trade associations to maintain and build international market share

**Market Access** – Marketing efforts can only be effective if foreign markets are open to BC products. Often this is not the case due to protectionist policies or regulations that do not recognize and accept North American standards. FII works with foreign governments to eliminate trade barriers and other restrictions to sales by:

- eliminating technical barriers that prevent or limit market access to BC forest products;
- encouraging use and acceptance of Canadian grading systems in new markets;
- encouraging recognition of BC products in foreign building codes and standards;
- teaching builders in foreign markets, through on-site training programs, how to build with BC forest products; and,
- identifying and addressing phyto-sanitary regulations and restrictions.

Product Development – BC's forest sector has a history of leadership both in developing new markets and commercializing new uses for wood products. The two factors are mutually supportive as new and innovative products and services are needed to meet changing market needs, provide a competitive advantage over products like concrete and steel, and differentiate BC from foreign competitors.

Through Product Development, FII partners with universities, researchers and the industry to conduct:

- technical research to demonstrate the superior quality of BC species and wood products;
- product testing to meet standards in overseas markets;
- applied research to adapt existing products or develop new products for emerging market needs; and,
- feasibility studies to assess new manufacturing techniques and the BC species most compatible with these new techniques.

**China Market Development** - Recognizing the importance of China in the global marketplace and the significant potential that China offers for wood products, FII has a separate program focused on researching and initiating projects to increase sales in China. In partnership with forest companies, associations and the Government of Canada's Canada Wood Export Program, FII uses an integrated marketing campaign that includes demonstration projects, promotional activities and local partnerships.

These demonstration projects include an 888 square metre demonstration centre that showcases BC wood products and wood construction technologies in Shanghai.

Future commercial partnerships will showcase hybrid construction (wood plus steel or concrete), renovation projects of existing Chinese buildings, and multi-storey, multi-family dwellings. Research and recent experience have confirmed that demonstration projects, combined with technical support, are the most effective way to achieve market development objectives in China.

**Mountain Pine Beetle** – FII has a major role in the Mountain Pine Beetle Emergency Response: Canada-BC Implementation Strategy announced in September, 2005. The plan supports forest communities and assists forest companies in recovering the greatest economic value from impacted timber.

FII's mandate within the plan is to develop a research and market development strategy that covers five areas:

- product development and technical research;
- product and market opportunity analysis;
- market access and phyto-sanitary issues;
- international customer communications; and,
- within-BC communications activities.

FII set up a mountain pine beetle program in the summer of 2005 and then hired a full-time program director. Operating out of Quesnel, in the middle of the region most impacted by the infestation, the director will manage stakeholder relations with industry and forest communities and lead efforts to develop product and market opportunities for MPB wood.

**Domestic Market Development** - While the majority of Market Development Business Area investments are focused on international markets, FII recognizes that pursuing opportunities within BC offers strong potential for market growth.

Program strategies within BC focus on providing resources to identify projects that could use wood instead of competing products like concrete or steel and support to overcome technical barriers, design requirements or engineering specifications required to expand wood use.

As part of this initiative, FII is supporting projects to increase the use of wood in the 2010 Olympic venues and the Vancouver Convention Centre. These high-profile venues will showcase BC wood products and advanced wood technologies to BC and the world.

FII also supports the competitiveness of the secondary manufacturing sector by identifying opportunities to improve manufacturing technology and process engineering and to transfer this technology to the sector.

### BC Market Outreach Network Program

Over the past 15 years, environmental campaigns have called into question a range of forest practices around the world. The campaigns have, in some cases, touched major forest-product buyers and caused some customers to review their buying patterns.

The BC Market Outreach Network Program (BCMON) is an in-house FII initiative that provides international buyers and others with credible facts documenting that BC forest products come from well-managed forests.

Environmental campaigns that promote misleading or incorrect information are quickly challenged by FII and its partners. They also monitor the development of draft legislation and procurement policies that could impair the flow of BC forest products into a particular market, making relevant officials aware of unintended consequences if the legislation or policy is adopted.

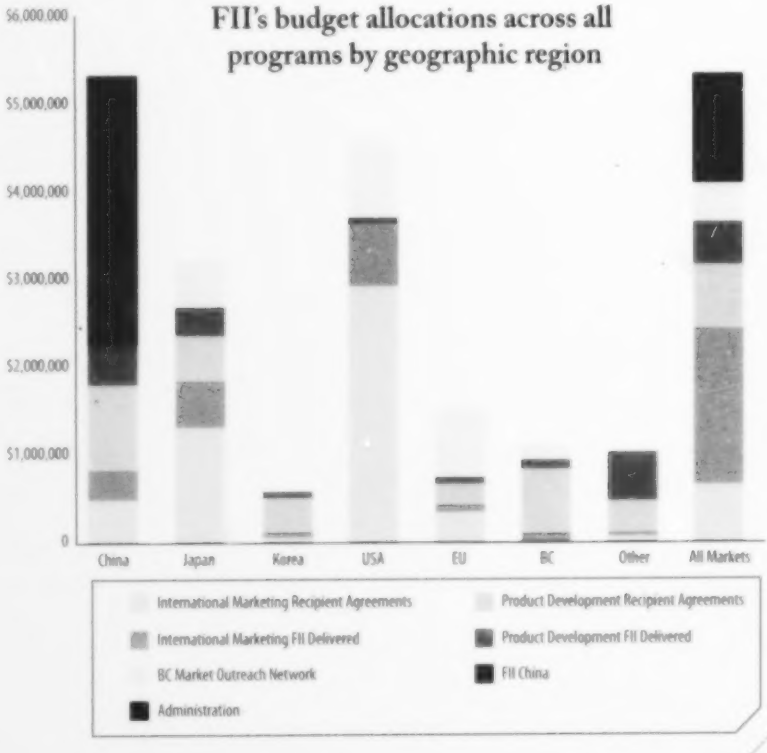
The program achieves its goals by:

- working with forest companies, trade associations, embassies and federal and provincial ministries to ensure a coordinated and strategic approach to market communications;
- gathering market research information about customers' environmental concerns which is used to support activities;
- distributing information materials, includ ing fact sheets and an up-to-date website www.bcforestinformation.com, to respond to market issues and changes in forest policy;
- attending major international trade shows to ensure customers and potential customers have information on BC's forests and environmental performance; and,
- leading the sector in on-going market monitoring to identify emerging issues and recommending and implementing a strategic response.

### Corporate support

Corporate support includes responsibility for the financial management and control of the corporation, information systems, human resources and performance management. Corporate services focus on internal management and employees, as well as serving the board of directors, government and partners by ensuring a high level of performance, accountability and adherence to government policies.

**FII's budget allocations across all programs by geographic region**



## STRATEGIC CONTEXT

### Vision

FII is an innovative and collaborative forest marketing support and funding agency that meets the needs of government, the BC forest industry, international markets and British Columbians.

### Mission

To support the BC forest industry with marketing, product development and factual information to ensure BC forest products are prized by and available to customers around the world.

### Values

**Positive Impact of Investments** – FII seeks an appropriate balance between short-term and longer-term public investments to optimize the rewards to British Columbia.

**Focus on Partnerships** – FII works in partnership with Canada and industry associations to ensure programs are efficiently delivered in a coordinated manner. FII encourages innovative programs and responses to changing circumstances.

**Integrity and Credibility** – Projects and services are delivered by capable, motivated individuals who focus on ensuring FII programs are credible and useful. FII staff learn from the past and improve the effectiveness and efficiency of FII programs by optimizing the use of resources, based on transparent decision-making and investment processes.

### Corporate locations

FII's corporate office is located at 1200 - 1130 West Pender Street in downtown Vancouver, British Columbia while the company's subsidiary office is located in Shanghai, China in the Dream Home Canada Demonstration Centre.

### China subsidiary

FII operates a subsidiary office in Shanghai, China called FII Consulting (Shanghai) Co., Ltd., (FII Shanghai). The company was set up in March 2004 and is registered in China to meet the legal requirements of the People's Republic of China. As a wholly foreign-owned enterprise, FII Shanghai is able to use facilities constructed in Shanghai to provide consulting services to FII and others, allowing FII to pursue its marketing and promotional activities in the Chinese market.

FII Shanghai is leading the development of demonstration projects in Shanghai, China. Each project is a vehicle to showcase BC wood products and forge inroads into the booming Chinese housing market through FII's China Market Development Program. The initiative is a collaboration with BC forest companies, the province through FII, China-based developer Shanghai Jinqiao Export Processing Zone Development Co. Ltd., Shanghai Municipal Housing and Land Bureau, Shanghai Science and Technology Committee and Shanghai's Xu Hui District.

Phase 1 of three phases was completed in January 2005 with the opening of Dream Home Canada, an 888 square metre (9,558 square feet) Demonstration Centre.

Progress is being made on Phase 2, the construction of two single-family homes, commonly known in China as villas, followed by apartment renovations and a multi-storey hybrid project of wood and concrete in Phase 3.

These projects are designed to demonstrate wood-frame construction, the flexibility of wood and the many wonderful qualities BC wood can bring to a structure. All three phases of the project are designed to further BC's efforts to penetrate this high-potential market with increased wood sales.

## CORPORATE GOVERNANCE

FII was incorporated on March 31, 2003 under the Business Corporations Act.

FII operates under an agreement with the Ministry of Forests and Range and is accountable to a board of directors.

The Board of Directors is supported by an audit committee which reviews, recommends and in some instances, approves financial statements and other financial information. Members of the committee are the:

- Deputy Minister of Finance;
- Assistant Deputy Minister of Management Services, Ministry of Economic Development; and,
- Assistant Deputy Minister of Corporate Services, Ministry of Forests and Range.

### Strategy Committee

FII is also supported by a strategy committee of seven senior executives from the Coastal and Interior forest industries representing primary and secondary manufacturing along with the remanufacturing sectors. The committee members meet regularly to provide

strategic advice to FII on programming, investments and organizational objectives.

FII's senior management team is comprised of the following members:

**Ken Baker,** Chief Executive Officer
**Karen Brandt,** Vice President, Market Communications
**Doug Greig,** Vice President, Finance and Administration
**Mike Hogan,** Vice President, China Operations
**Michael Loseth,** Vice President, International Marketing

Forestry Innovation Investment Ltd. is committed to the following principles to guide its activities and delivery of services:

**Accountability** – Establishing structures and processes, setting performance-based standards and measures, and implementing compliance monitoring, auditing and reporting to enable and demonstrate cost-effective progress towards FII goals and objectives.

**Competitiveness and Innovation** – Ensuring that British Columbia remains internationally competitive by improving the value derived from BC's forest land asset. This involves investments that encourage innovative approaches, technologies and skills and improve manufacturing processes and products, as well as marketing and communication activities to increase BC's market share in both new and existing markets.

**Continuous improvement** – Learning from the past and improving the effectiveness and efficiency of FII programs, by optimizing the use of resources by recipients and FII.

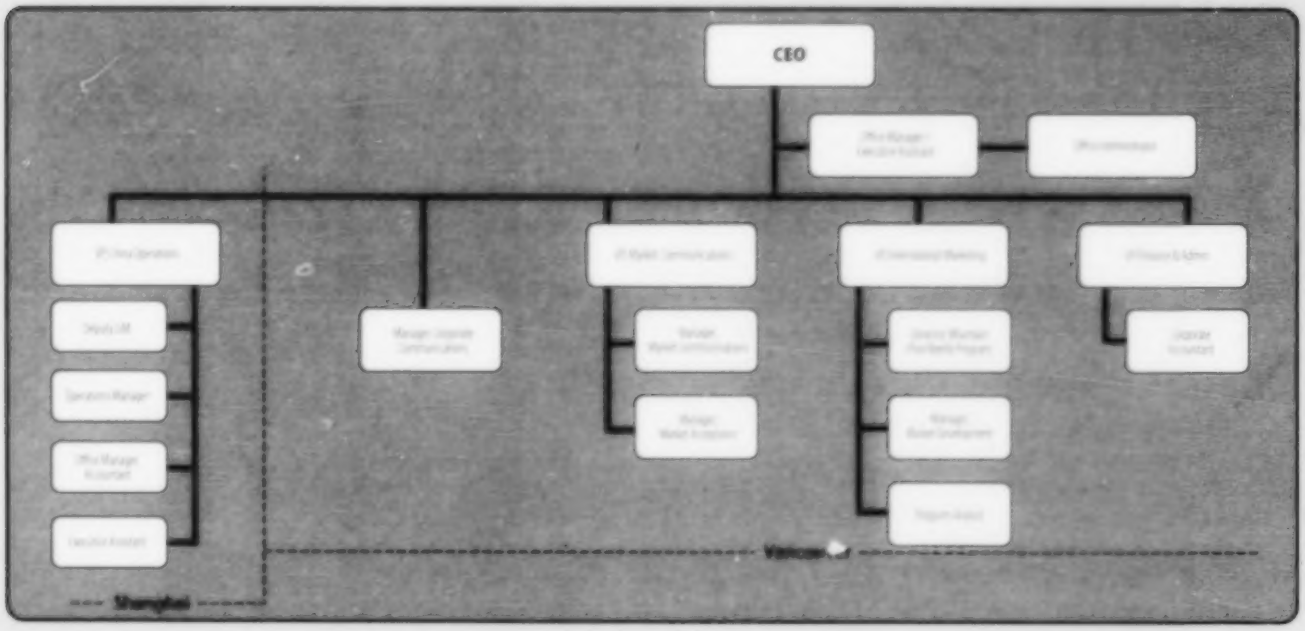
**Knowledge-based decision-making** – Making informed decisions built on current, accurate market-based information and risk assessment.

**Transparency** – Establishing open and understandable decision-making and investment processes, and ensuring that FII policies on competitive tendering are applied, and regular performance reporting is conducted.

**Positive Return on Investment** – Ensuring that FII investments optimize the return to British Columbia based on an appropriate balance between short-term and longer-term objectives.

**Working in Partnership** – Working in partnership with internationally recognized associations to ensure that FII services and functions can be efficiently delivered in a coordinated manner and to ensure that funds are used to address priority issues and needs of the forest sector.

The Minister of Forests and Range is responsible for FII.



FII's September 2005 Service Plan Update set the following four goals:

**Goal 1:** Increased demand for BC wood products.
**Goal 2:** An international reputation as a leader in sustainable forest management
**Goal 3:** A coordinated approach to market development that optimizes partner and recipient contributions.
**Goal 4:** An effective, well-managed organization.

To varying degrees, achieving these goals depends on factors FII cannot control, such as global trade developments, exchange rates, global security issues and local political climates. Forest and land-use policy developments can also affect the scope and design of some FII investments, or lead to new priorities.

## Increased demand for BC wood products.

2005/06 was a challenging year for BC forestry exports. The high value of the Canadian dollar and increasing transportation costs made it more difficult to be price-competitive in many markets. In particular, aggressive pricing by foreign competitors in Asian markets compounded these factors.

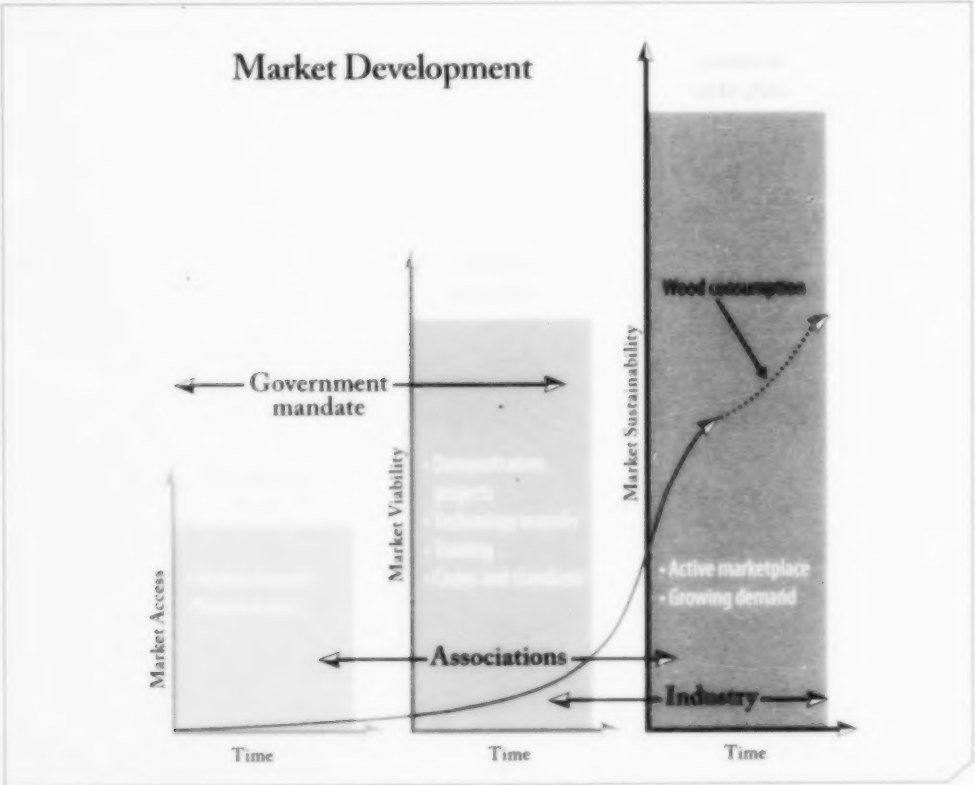
These pressures were more than offset by a strong U.S. market. The damage from Hurricane Katrina and other natural disasters, as well as a continuing strength in the housing sector created strong demand for BC structural lumber and panel products.

FII's Market Development programs supported market presence with activities focused on three objectives:

- tackling market barriers;
- enhancing the competitiveness of wood products manufacturers; and,
- improving customer awareness and interest through effective marketing.

All programs focus on adding value and delivering tangible benefits to the industry by working with forestry associations and partners rather than duplicating their efforts. This means doing work that the sector cannot do on its own, and targeting investments at the most appropriate points in the market development cycle:

FII's market-development investments are largely used to fund projects carried out by the industry associations and research and academic institutes in the development and emerging phases illustrated above. Much of that work is partly funded by the federal government while FII undertakes some projects directly. FII does not fund commercial market activities because it does not provide subsidies.



strategic advice to FII on programming, investments and organizational objectives.

FII's senior management team is comprised of the following members:

**Ken Baker,** Chief Executive Officer
**Karen Brandt,** Vice President, Market Communications
**Doug Greig,** Vice President, Finance and Administration
**Mike Hogan,** Vice President, China Operations
**Michael Loseth,** Vice President, International Marketing

Forestry Innovation Investment Ltd. is committed to the following principles to guide its activities and delivery of services:

**Accountability** – Establishing structures and processes, setting performance-based standards and measures, and implementing compliance monitoring, auditing and reporting to enable and demonstrate cost-effective progress towards FII goals and objectives.

**Competitiveness and Innovation** – Ensuring that British Columbia remains internationally competitive by improving the value derived from BC's forest land asset. This involves investments that encourage innovative approaches, technologies and skills and improve manufacturing processes and products, as well as marketing and communication activities to increase BC's market share in both new and existing markets.

**Continuous improvement** – Learning from the past and improving the effectiveness and efficiency of FII programs, by optimizing the use of resources by recipients and FII.

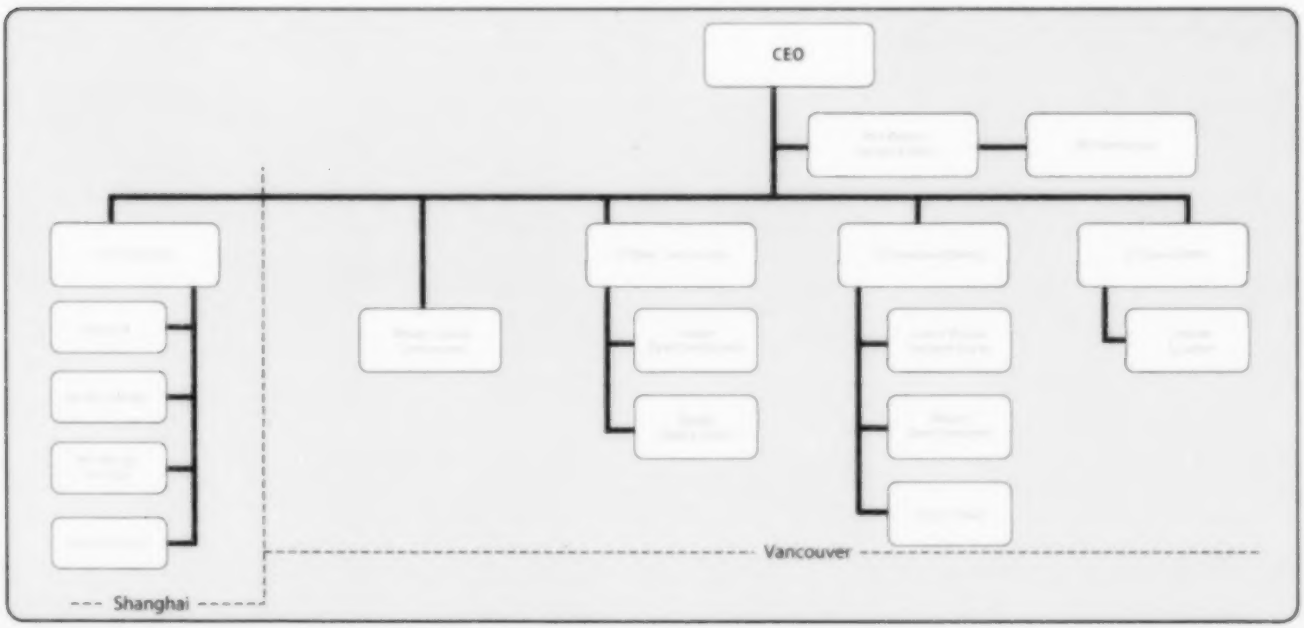
**Knowledge-based decision-making** – Making informed decisions built on current, accurate market-based information and risk assessment.

**Transparency** – Establishing open and understandable decision-making and investment processes, and ensuring that FII policies on competitive tendering are applied, and regular performance reporting is conducted.

**Positive Return on Investment** – Ensuring that FII investments optimize the return to British Columbia based on an appropriate balance between short-term and longer-term objectives.

**Working in Partnership** – Working in partnership with internationally recognized associations to ensure that FII services and functions can be efficiently delivered in a coordinated manner and to ensure that funds are used to address priority issues and needs of the forest sector.

The Minister of Forests and Range is responsible for FII.



FII's September 2005 Service Plan Update set the following four goals:

**Goal 1:** Increased demand for BC wood products.
**Goal 2:** An international reputation as a leader in sustainable forest management
**Goal 3:** A coordinated approach to market development that optimizes partner and recipient contributions.
**Goal 4:** An effective, well-managed organization.

To varying degrees, achieving these goals depends on factors FII cannot control, such as global trade developments, exchange rates, global security issues and local political climates. Forest and land-use policy developments can also affect the scope and design of some FII investments, or lead to new priorities.

2005/06 was a challenging year for BC forestry exports. The high value of the Canadian dollar and increasing transportation costs made it more difficult to be price-competitive in many markets. In particular, aggressive pricing by foreign competitors in Asian markets compounded these factors.

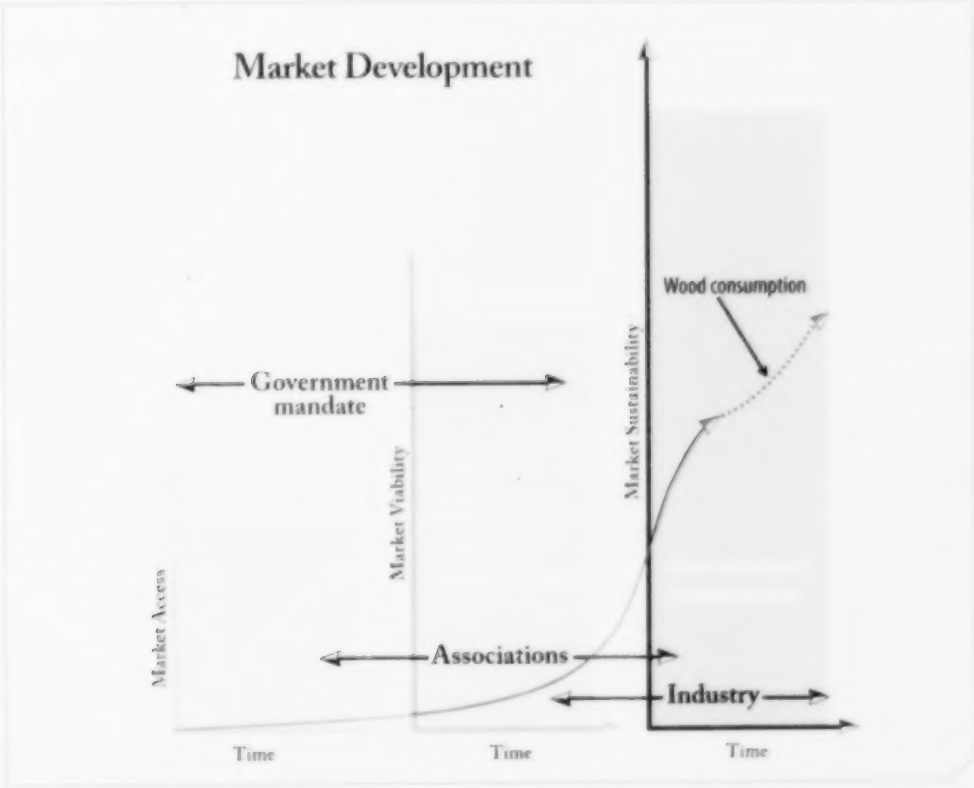
These pressures were more than offset by a strong U.S. market. The damage from Hurricane Katrina and other natural disasters, as well as a continuing strength in the housing sector created strong demand for BC structural lumber and panel products.

FII's Market Development programs supported market presence with activities focused on three objectives:

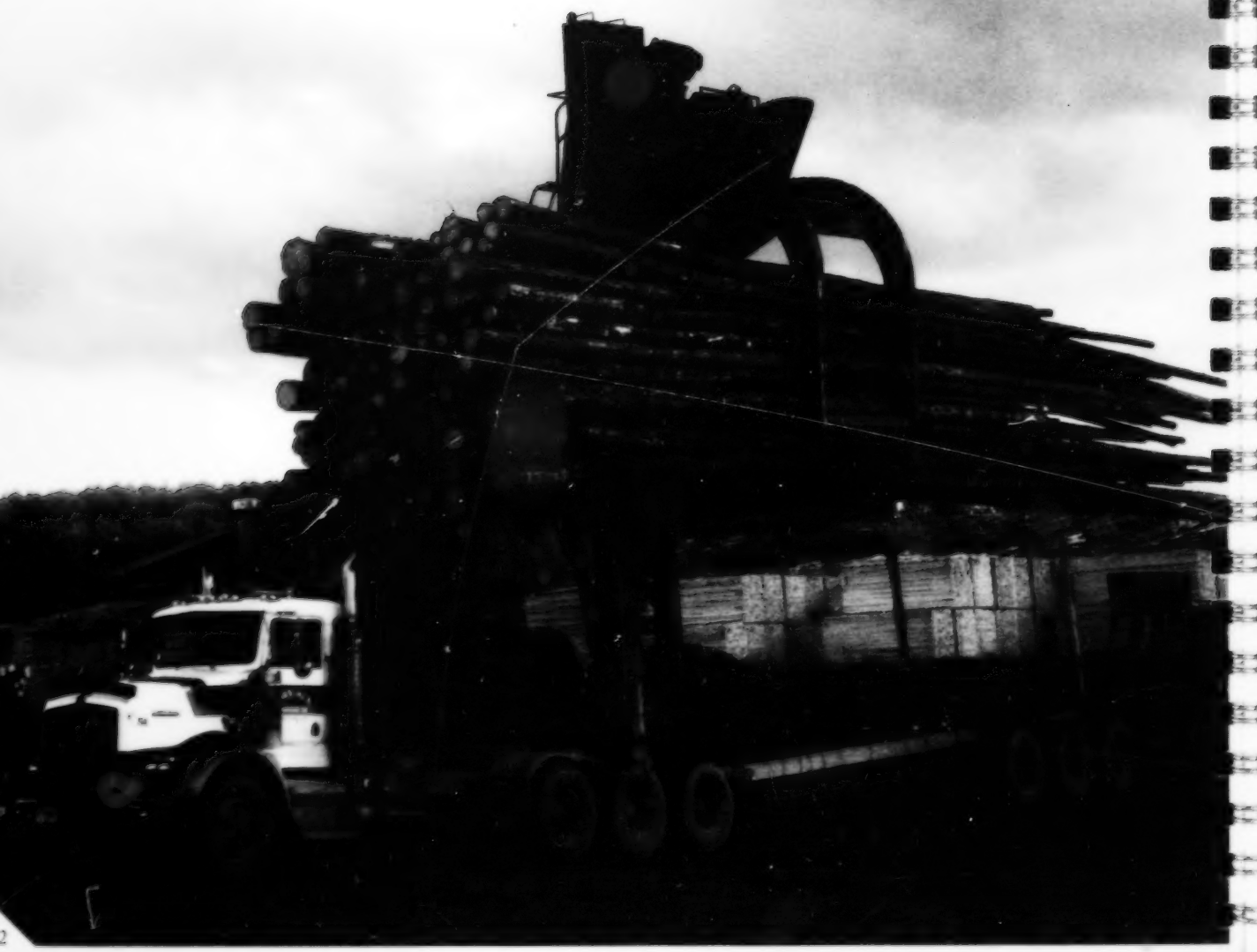
- tackling market barriers;
- enhancing the competitiveness of wood products manufacturers; and,
- improving customer awareness and interest through effective marketing.

All programs focus on adding value and delivering tangible benefits to the industry by working with forestry associations and partners rather than duplicating their efforts. This means doing work that the sector cannot do on its own, and targeting investments at the most appropriate points in the market development cycle:

FII's market-development investments are largely used to fund projects carried out by the industry associations and research and academic institutes in the development and emerging phases illustrated above. Much of that work is partly funded by the federal government while FII undertakes some projects directly. FII does not fund commercial market activities because it does not provide subsidies.



In 2005, BC exports of commodity wood products were 35.8 million cubic metres, 4% more than the 34.5 million cubic metres of exports in 2004



Maintain or improve access to international markets for BC wood product manufacturers

In 2005/06 The Market Development Programs focused on dismantling trade barriers in key Asian markets, including Japan, Korea and China. These barriers included formal restrictions such as phytosanitary controlstory barriers and technical bottlenecks, such as restrictions on wood use in building and fire codes.

Given the complexities of Asian markets, an inventory of market barriers and Market Access Index were developed. The index will be used in future years to measure progress against the challenges to market access.

The coordinated efforts in Asia achieved a number of significant milestones:

- **Korea** upgraded its building code and approved a major expansion in the use of wood-frame construction to four-storey residential buildings. This change opens up an important part of the multi-family residential market to wood-frame design. Since Korea imports almost all of its structural wood, this market is a growth opportunity for BC forest products.

- **China** - Significant progress on the implementation of a new national building code that will allow western style, wood-frame construction and greater wood use in renovations. Retrofitting old apartment blocks to modern energy standards, and replacing aging roofing, together represent a multi-billion dollar potential for wood products.

- Research conducted on the market potential for renovation work in Shanghai determined there is 26.1 million square metres of housing still to be renovated. This figure encompasses two potentially large niche opportunities including sloped roof renovations and renovation projects involving the addition of an extra storey of living space on former public housing structures. Together these represent an upper limit market opportunity for wood of nearly $200 million in Shanghai alone.

- FII Shanghai will undertake a roof renovation project that will link closely with the Shanghai code-development process and serve as a model for code experts to identify and address gaps in the code related to use of wood in renovation.

- In September 2005, supported by the Canada Wood Group, the American Forest and Paper Association, European Wood and China's Tianjin Fire Research Institute, an agreement was signed for a joint review of China's existing fire-safety requirements covering use of wood in construction. The Joint Technical Review Committee is charged with studying how existing Chinese requirements may be aligned with internationally recognized fire-safety engineering principles. The Council of Forest Industries, with FII and Government of Canada funding, was instrumental in initiating this important project.

- Technical transfer programs including the Quality Assurance Program and seminar series are in place to provide support to designers, builders and developers with the goal of improving understanding, expertise and the quality of wood-frame projects in China. The Canada Wood Group technical team has been active in supporting 10 builders, half of whom are new to wood-frame construction in the past year.

- **Japan**: Research into a new kiln-dried hemlock product for post and beam construction was completed and is now being reviewed by Japanese technical authorities. Once approved, this will provide BC's coastal forest sector with a new product line in its largest export market.

Position BC as a leader in wood product development, quality and manufacturing efficiency

BC has a history of developing new markets and introducing new products and manufacturing systems to keep the provincial sector at the forefront of harvesting, milling and value-added technologies.

The mountain pine beetle infestation, in particular, requires innovative solutions. FII is leading the efforts to find ways to make mountain pine beetle wood a profitable and economically viable source of fibre.

In 2005/2006, 15 projects totalling more than $1 million were funded to study, among other things:

- fibre quality and shelf life;
- improving manufacturing efficiencies and lumber recovery;
- bleaching out the blue stain caused by the beetle;
- researching and applying preservative treatments for use in outdoor and landscaping products; and
- increasing moisture content to produce better quality fibre strands for structural panels.

The projects were designed to determine how beetle-attacked timber can be used to its fullest potential by testing its viability in a variety of product applications such as laminated decking and flooring, structural panels and particleboard, structural beams made of laminated wood, and other products.

FII also directly initiated a number of complementary trials and studies using MPB fibre including:

- testing railway ties from grey-stage MPB fibre for creosote treating and analysis by the Chinese Academy of Forestry; and,
- conducting a market study of railway tie demands in China in the future.

The study of the Chinese railway tie market was designed to examine the market's potential as a new opportunity including market size, opportunities and challenges. The report found the trend in China is to use wooden ties in only specialized situations. It also identified current suppliers and price points as well as purchase criteria.

Along with MPB-related activities, the Product Development Program invested in a technology-transfer program to improve operating efficiency and productivity in secondary wood products manufacturing. Through consulting services provided by Forintek Canada's Solutions for Wood program, funded by FII, staff worked on 30 company-specific technical projects, made 324 site visits to value-added facilities across the province and responded to 57 technical inquiries while 13 technical seminars attracted over 340 participants.

The Solutions for Wood initiative worked with a wide range of companies in 2005/2006 including kitchen-cabinet manufacturers, wood-flooring producers, lumber remanufacturers and log and timber-frame home builders.

The program provided in-plant assessments of technical needs and opportunities, solved specific technical problems, responded to technical enquiries over the phone and provided technical literature addressing common industry problems.

The impact of these activities has been significant. An analysis of companies sampled in 2005/2006 identified considerable benefit as a result of technical assistance, as measured by cost savings in materials, increased manufacturing efficiencies, new products developed and higher sales volumes.

Based on the sample, companies experienced an average return on investment (ROI) of 10 to 1 when technical improvements were implemented. More significantly, investments by the individual companies experienced a six-month payback period.

FII provides marketing information on BC's forest products and wood species to support various marketing campaigns and to respond to inquiries from customers and consumers around the world.

More than 86,000 users visited bcforestproducts.com, which features product information, details on wood species and links to forestry companies, associations and information about BC's sustainable forest policies. Ninety percent of the site's visitors are from outside BC.

FII also released the Buyer's Guide to British Columbia Wood Products, a one-stop source of information about the BC wood industry with details on wood species, wood use, the diversity of the province's forests, as well as BC's commitment to sustainable forest management. The guide has been extremely well received through its distribution at tradeshows and other promotional events.

FII continues to promote BC forestry through a major presence at key international tradeshows. Over the past year, over 14,000 people visited the FII exhibit at shows in the U.S., China and Japan. The program is developed in co-operation with the Canada Wood Export Program and in 2005/06 included participation from eight forest industry trade associations and 21 individual companies.

FII continues to evaluate and monitor the impact and effectiveness of its tradeshow activities – third-party evaluations completed indicated that 70% of visitors were more likely to purchase BC wood products after visiting the coordinated BC Wood Products Showcase.

The following highlights show the gains made in various markets:

- **United States** – Sales of BC forest products in the United States increased by 1.4% in 2005/06 with small to medium growth in all product categories. Reconstruction in the gulf coast following hurricane Katrina increased demand for structural wood and panelling, with MDF (up 7.3%) and OSB (up 2.7%) showing the greatest gains.

FII also directly initiated a number of complementary trials and studies using MPB fibre including:

- testing railway ties from grey-stage MPB fibre for creosote treating and analysis by the Chinese Academy of Forestry; and,
- conducting a market study of railway tie demands in China in the future.

The study of the Chinese railway tie market was designed to examine the market's potential as a new opportunity including market size, opportunities and challenges. The report found the trend in China is to use wooden ties in only specialized situations. It also identified current suppliers and price points as well as purchase criteria.

Along with MPB-related activities, the Product Development Program invested in a technology-transfer program to improve operating efficiency and productivity in secondary wood products manufacturing. Through consulting services provided by Forintek Canada's Solutions for Wood program, funded by FII, staff worked on 30 company-specific technical projects, made 324 site visits to value-added facilities across the province and responded to 57 technical inquiries while 13 technical seminars attracted over 340 participants.

The Solutions for Wood initiative worked with a wide range of companies in 2005/2006 including kitchen-cabinet manufacturers, wood-flooring producers, lumber remanufacturers and log and timber-frame home builders.

The program provided in-plant assessments of technical needs and opportunities, solved specific technical problems, responded to technical enquiries over the phone and provided technical literature addressing common industry problems.

The impact of these activities has been significant. An analysis of companies sampled in 2005/2006 identified considerable benefit as a result of technical assistance, as measured by cost savings in materials, increased manufacturing efficiencies, new products developed and higher sales volumes.

Based on the sample, companies experienced an average return on investment (ROI) of 10 to 1 when technical improvements were implemented. More significantly, investments by the individual companies experienced a six-month payback period.

FII provides marketing information on BC's forest products and wood species to support various marketing campaigns and to respond to inquiries from customers and consumers around the world.

More than 86,000 users visited bcforestproducts.com, which features product information, details on wood species and links to forestry companies, associations and information about BC's sustainable forest policies. Ninety percent of the site's visitors are from outside BC.

FII also released the Buyer's Guide to British Columbia Wood Products, a one-stop source of information about the BC wood industry with details on wood species, wood use, the diversity of the province's forests, as well as BC's commitment to sustainable forest management. The guide has been extremely well received through its distribution at tradeshows and other promotional events.

FII continues to promote BC forestry through a major presence at key international tradeshows. Over the past year, over 14,000 people visited the FII exhibit at shows in the U.S., China and Japan. The program is developed in co-operation with the Canada Wood Export Program and in 2005/06 included participation from eight forest industry trade associations and 21 individual companies.

FII continues to evaluate and monitor the impact and effectiveness of its tradeshow activities – third-party evaluations completed indicated that 70% of visitors were more likely to purchase BC wood products after visiting the coordinated BC Wood Products Showcase.

The following highlights show the gains made in various markets:

- **United States** – Sales of BC forest products in the United States increased by 1.4% in 2005/06 with small to medium growth in all product categories. Reconstruction in the gulf coast following hurricane Katrina increased demand for structural wood and panelling, with MDF (up 7.3%) and OSB (up 2.7%) showing the greatest gains.

- Promotion of BC Cedar products in the United States achieved a number of milestones in 2005/06 with builder consumption of BC products up 5.3%. The Cedar Shake and Shingle Bureau responded to marketplace pressures in the US with a campaign that reached more than 3.2 million consumers, 900 insurance industry officials and led to fewer municipalities moving to restrict cedar roofing. The outreach program was so effective that the bureau was invited by the insurance industry to participate in the reconstruction planning of the gulf region.

- The Western Red Cedar Lumber Association reached more than 115 million American consumers through a combination of news coverage, participation in home renovation and other specialty TV shows, targeted advertising, and trade shows in all major regions of the U.S. The association estimates increased sales of $12.25 million from the campaign, generating an ROI for FII's investment of 744%.

- **Japan** – BC sales were strong in a relatively weak Japanese market. This performance reflects the on-going work by COFI, funded by FII, to maintain a high profile for BC products through trade and business-to-business marketing. A record 96,000 2x4 housing starts combined with strengthening economic forecasts for Japan, indicate continued demand for BC's spruce/pine/fir (SPF) products. Prospects for Coastal post and beam hemlock products, however, continue to decline.

- **China** – With strong North American demand, a high Canadian dollar and increasing international competition, sales of BC forest products to China dropped 3.3% in 2005/06. OSB, MDF and particleboard sales grew but sales of softwood plywood and lumber fell modestly. Despite the decline this year, the market has grown a hefty 274% since 2001 and remains a significant growth market for BC wood products and an area of major investment for FII. Through a partnership with the Canada Wood Export Program, industry associations and others in China, FII has developed a comprehensive strategy that aims to increase market acceptance and demand for BC wood products in this important emerging market.

  While the focus remains heavily on market-access activities such as building codes, technology transfer and quality assurance, working under the Canada Wood Group marketing umbrella, the China partners have:

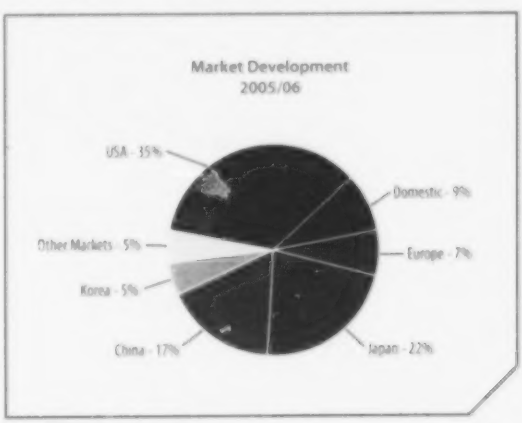
  - held more than 30 events, training and technical seminars, and discussions at the Dream Home Canada Demonstration Centre;
  - served as an initial contact point for builders looking for information and advice on wood-frame construction and building with wood;
  - attended two major tradeshows attracting over 8,000 visitors to the display; and,
  - formed partnerships with local government agencies to develop a wood truss roof renovation project that will be used to establish standards for the commercialization of this technology.

- **Europe** – Since the Western Red Cedar Export Association began a marketing program in 2003, shipments to Europe have increased 32.3% over 2002 levels. The campaign targets architects and the home design sector through direct mail, targeted advertising in trade magazines, an updated image library, Internet promotion and an online training tool.

- **Australia/New Zealand** – The Western Red Cedar Association's Real Cedar promotional campaign in Australia and New Zealand was very successful with a three-fold increase in site visits to the association's web site and more than 1,200 direct business leads.

- **North America** – The Canadian Wood Council (CWC) has been promoting advanced wood technology for commercial buildings through a communication program targeted to architects, developers and planners. In 2005/06 this campaign reached more than 320,000 professionals across Canada.

The following chart shows the percentage of recipient funding invested in target markets:



**Exit interviews from the FII booth at the International Building Show in Florida found 97 per cent of respondents felt BC forest management is very positive or positive**

British Columbia positioned as a global leader in sustainable forest management.

## Promoting British Columbia's coast vision

In February 2006, British Columbia attracted international attention when it announced the land use decisions for its north and central Pacific Coast regions, also known as the Great Bear Rainforest. After nearly 10 years of multi-stakeholder planning, the consensus agreements reinforced British Columbia's position as a leader in forest management by showing that diverse groups can work together to solve tough land-management issues.

FII worked with the British Columbia government, the forest industry and environmental organizations to celebrate this achievement with international customers, including some who had taken a close interest in the planning processes. FII:

- prepared and distributed a summary fact sheet to Canadian embassies and international markets;
- partnered with the Coast Forest Conservation Initiative, which represents major forest companies on the coast, to produce a customer marketing package titled Beyond Expectations: A New Beginning in the Rainforest which includes a publication, brochure and DVD; and,
- sent the materials to a wide international audience as well as posting both in a new coast section on its website, www.bcforestinformation.com

FII will continue to keep international markets informed as the coast land use planning decisions take effect, including the introduction of ecosystem-based management.

## Measuring market acceptance

Formal customer surveys in 2004/05 indicated an average 70 per cent customer acceptance of new and existing wood products from British Columbia. The 2005/06 FII September Service Plan Update target was to increase this customer acceptance to 80 per cent in 2007/08 and maintain this acceptance level.

FII has since refined this target and will focus on implementing broader recommendations from its customer research. The survey results will continue to help direct FII activities and ensure customer acceptance of British Columbia forest practices and products remains strong.

Research from two U.S. trade shows in 2005/06 showed that approval for British Columbia products and practices remains high. Exit interviews from the FII booth at the International Building Show in Florida found that 97 per cent of respondents felt British Columbia's forest management is very positive or positive, and 84 per cent were confident British Columbia forest products are an environmentally responsible choice. At the GreenBuild show in Atlanta, 75 per cent reported positive or very positive support for British Columbia forest management and 87 per cent confidence in forest products.

## Reaching out to markets

In 2005/06, FII looked for ways to strengthen British Columbia's international reputation as a responsible forest manager. This often meant providing information for individuals or organizations in a position to become advocates for the British Columbia forest sector. For example, FII and partners arranged outreach sessions for Canadian consulate representatives in the United States, Europe and Asia, and will follow up with forest tours in British Columbia for some participants in 2006/07.

Facts about British Columbia forest management and sustainability were also delivered directly to customers and decision makers at high-profile international events and trade shows, and FII staff made presentations to forest products buyers in countries such as Japan and Holland.

FII participated in the inaugural Global Forest and Paper Industry summit and the World Wildlife Fund (WWF) international AGM, which discussed sustainability issues. It was represented at key trade shows including Interzum 2005 in Germany, the Japan Home Show and the Pacific Coast Builders Conference (PCBC) 2005 in San Francisco. FII shared its best practices as part of an international networking forum of communications specialists involved in promoting wood products and forests.

In-market activities often result in opportunities to invite customers to British Columbia for a first-hand look at the province's forest management. In 2005/06, FII was involved in seven forest tours that brought more than 100 customers and influencers from Japan, Germany and the United Kingdom to British Columbia.

In 2005/06, FII prepared new fact sheets on the central and north coast land use decisions and old-growth forests, and updated existing materials on forest certification and protecting species at risk. It significantly increased its library of still photography and video footage to improve the quality of its own materials and those of its many partners.

FII produced the video wall for British Columbia-Canada Place at the 2006 Olympic and Paralympic Winter Games in Turin, Italy. The building attracted more than 100,000 visitors and journalists.

In spring 2005, FII created three forestry information kiosks for the Tsawwassen Quay Market, the only non-commercial activities in the new market area in the BC Ferries Tsawwassen terminal. More than 3.25 million tourists and British Columbia vehicle passengers travel through the terminal each year.

Market research commissioned by FII in 2005/06 found that architects and trade show participants interviewed in the United States believe the green building trend is growing, and will continue to grow in that country. This fits with FII activities aimed at assuring customers that forest products, especially those from British Columbia's well-managed forests, are an excellent choice for the environment.

In 2005/06, FII unveiled a Guide to Buying Green website and publication that shows architects, customers and planners the environmental benefits of building with wood, and helps them develop procurement policies that offer both flexibility and assurance that the wood products they are buying meet the best environmental standards.

Along with many Canadian forest sector partners, FII is advocating more flexibility and more emphasis on the use of lifecycle analysis (which benefits wood) as part of the U.S. Green Building Council's LEED (Leadership in Energy and Environmental Design) building standard. It officially responded to proposed legislation in a number of U.S. jurisdictions that could have had a negative impact on the use of British Columbia wood. Three of the statutes were withdrawn.

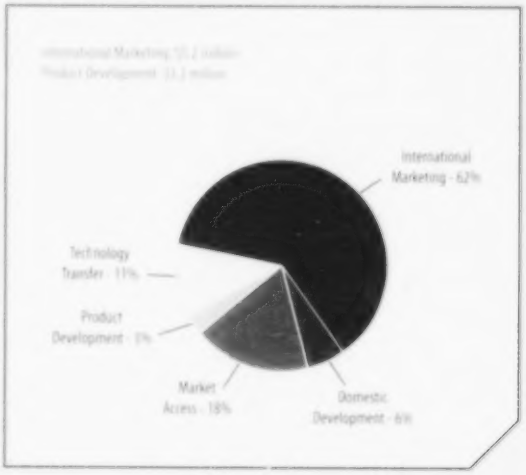
FII was represented at a summit of the American Institute of Architects in Washington D.C., to discuss options for a sustainable building standards policy and a summit arranged by the U.S. Green Building Council to improve understanding of LEED's sustainability criteria.

British Columbia has more certified lands than any other jurisdiction except for all of Canada – most is certified to the Canadian Standards Association's Sustainable Forest Management Standard and the Sustainable Forestry Initiative and a small amount is certified to the Forest Stewardship Council. Both CSA and SFI have been endorsed by PEFC (the Programme for the Endorsement of Forest Certification), the world's largest forest certification umbrella organization.

British Columbia's leadership in forest certification is an important indicator of good forest management practices for international customers. FII is involved in a number of activities to promote and explain the value of certification and to improve acceptance of all three of the globally recognized programs used in British Columbia.

One example is in China where there is growing pressure for certified forests and forest products, which has led to a move to develop a Chinese national forest certification standard. FII is working with Canadian associations and representatives from other major producing jurisdictions, including the United States, Sweden, Finland and Australia to encourage Chinese acceptance of forest certification standards endorsed by both PEFC and FSC.

A partnered approach to market development is fundamental to industry success. In 2005/06, FII contributed $8.4 million to partnered activities to develop markets and products. The following graphic shows the proportion of funding dedicated to the various market-development activities.




FII's Market Development programs invested over $8 million for activities in key export markets in 2005/06, including 44 projects conducted by 15 industry, research and development organizations, as well as a comprehensive, coordinated trade show strategy.

In spring 2005, FII created three forestry information kiosks for the Tsawwassen Quay Market, the only non-commercial activities in the new market area in the BC Ferries Tsawwassen terminal. More than 3.25 million tourists and British Columbia vehicle passengers travel through the terminal each year.

Market research commissioned by FII in 2005/06 found that architects and trade show participants interviewed in the United States believe the green building trend is growing, and will continue to grow in that country. This fits with FII activities aimed at assuring customers that forest products, especially those from British Columbia's well-managed forests, are an excellent choice for the environment.

In 2005/06, FII unveiled a Guide to Buying Green website and publication that shows architects, customers and planners the environmental benefits of building with wood, and helps them develop procurement policies that offer both flexibility and assurance that the wood products they are buying meet the best environmental standards.

Along with many Canadian forest sector partners, FII is advocating more flexibility and more emphasis on the use of lifecycle analysis (which benefits wood) as part of the U.S. Green Building Council's LEED (Leadership in Energy and Environmental Design) building standard. It officially responded to proposed legislation in a number of U.S. jurisdictions that could have had a negative impact on the use of British Columbia wood. Three of the statutes were withdrawn.

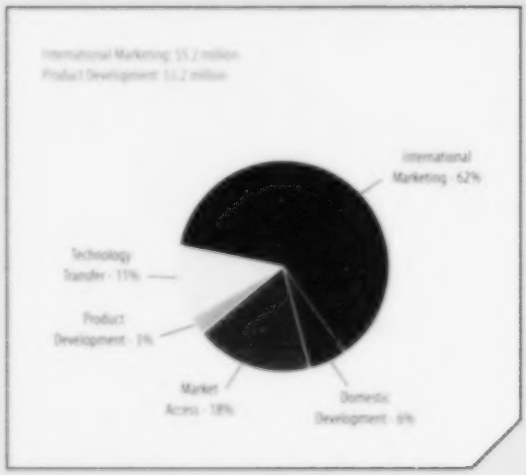
FII was represented at a summit of the American Institute of Architects in Washington D.C., to discuss options for a sustainable building standards policy and a summit arranged by the U.S. Green Building Council to improve understanding of LEED's sustainability criteria.

British Columbia has more certified lands than any other jurisdiction except for all of Canada – most is certified to the Canadian Standards Association's Sustainable Forest Management Standard and the Sustainable Forestry Initiative and a small amount is certified to the Forest Stewardship Council. Both CSA and SFI have been endorsed by PEFC (the Programme for the Endorsement of Forest Certification), the world's largest forest certification umbrella organization.

British Columbia's leadership in forest certification is an important indicator of good forest management practices for international customers. FII is involved in a number of activities to promote and explain the value of certification and to improve acceptance of all three of the globally recognized programs used in British Columbia.

One example is in China where there is growing pressure for certified forests and forest products, which has led to a move to develop a Chinese national forest certification standard. FII is working with Canadian associations and representatives from other major producing jurisdictions, including the United States, Sweden, Finland and Australia to encourage Chinese acceptance of forest certification standards endorsed by both PEFC and FSC.

A partnered approach to market development is fundamental to industry success. In 2005/06, FII contributed $8.4 million to partnered activities to develop markets and products. The following graphic shows the proportion of funding dedicated to the various market-development activities.




FII's Market Development programs invested over $8 million for activities in key export markets in 2005/06, including 44 projects conducted by 15 industry, research and development organizations, as well as a comprehensive, coordinated trade show strategy.

More than 93% of the projects leveraged funding from other sources such as industry and the Government of Canada's Canada Wood Export Program, bringing the total value of the projects to over $20 million. In addition, over 61% of the projects leveraged funding from two or more sources.

Overall, activities carried out by others were funded as follows[1]:

**FII** – 44.2%
**Government of Canada**[2] – 22.3%
**Industry**[3] – 33.5%

### Increased co-ordination among forest sector partners

Through the Canada Wood Export Program (CWEP), the federal government is an important partner in the international marketing of BC and Canadian wood products. FII has developed an effective working relationship with CWEP and together coordinated and completed the development of an online Web application system to link proposed projects to common market strategies. This coordinated approach helped streamline the call for proposals process and data collection.

FII and CWEP support the development of the Canada Wood brand outside of North America since Canada's national profile is higher than provincial or regional profiles in foreign markets. FII recognizes this and is encouraging associations and groups from other provinces to use the Canada Wood brand as a means of differentiating Canadian wood products from foreign competitors.

At Dream Home Canada in Shanghai, the formation of the Canada Wood Group partnership is helping to streamline costs, optimize human resources and create efficiencies. Through a joint planning process, the Canada Wood partners have embarked on a three-year market plan to focus activities on technology transfer, quality assurance and other market outreach while continuing to demonstrate the many benefits of wood-frame construction through demonstration projects.

A Dream Home Canada inquiry management process was also developed to record, categorize and forward incoming requests for handling by the appropriate trade association rep or technical expert. Passing each contact through a review process has proven effective in qualifying inquiries and uncovering opportunities beyond what was originally requested.

A joint CWG/FII technical team was also established to provide coordinated handling of technical inquiries and support for builders and developers. Operating out of the new Canada Wood Technical Support Centre inside Dream Home Canada, this team is at the core of the CWG Quality Assurance Program aimed at raising the capacity and standards of wood frame construction in China.

With the development of the Canada Wood Group partnership and the increasing business opportunities in China, FII has funded an assesssment of the technicalities involved in potentially establishing a Canada Wood Group legal entity in China which will allow for more fulsome business activities. The legal discussions are continuing with and on behalf of the trade association members of the consortium.

FII also encouraged greater collaboration between several of BC's cedar product producers in 2005/06. With greater strength in marketing and market presence, the BC Shake and Shingle Association joined forces with BC Wood Specialties Group, the Western Red Cedar Lumber Association and the Western Red Cedar Export Association on several marketing initiatives that gave greater profile and impact to this important segment of the BC industry.

### An effective, well managed organization

In 2005/06, FII commissioned an independent review of forest sector satisfaction with FII's programs and operations. The survey canvassed senior officials in forestry companies, trade associations, embassies and government. A majority of participants gave FII very favourable ratings and more than nine in 10 people said FII has improved significantly in the past two years, with many citing greater collaboration and partnership on key issues.

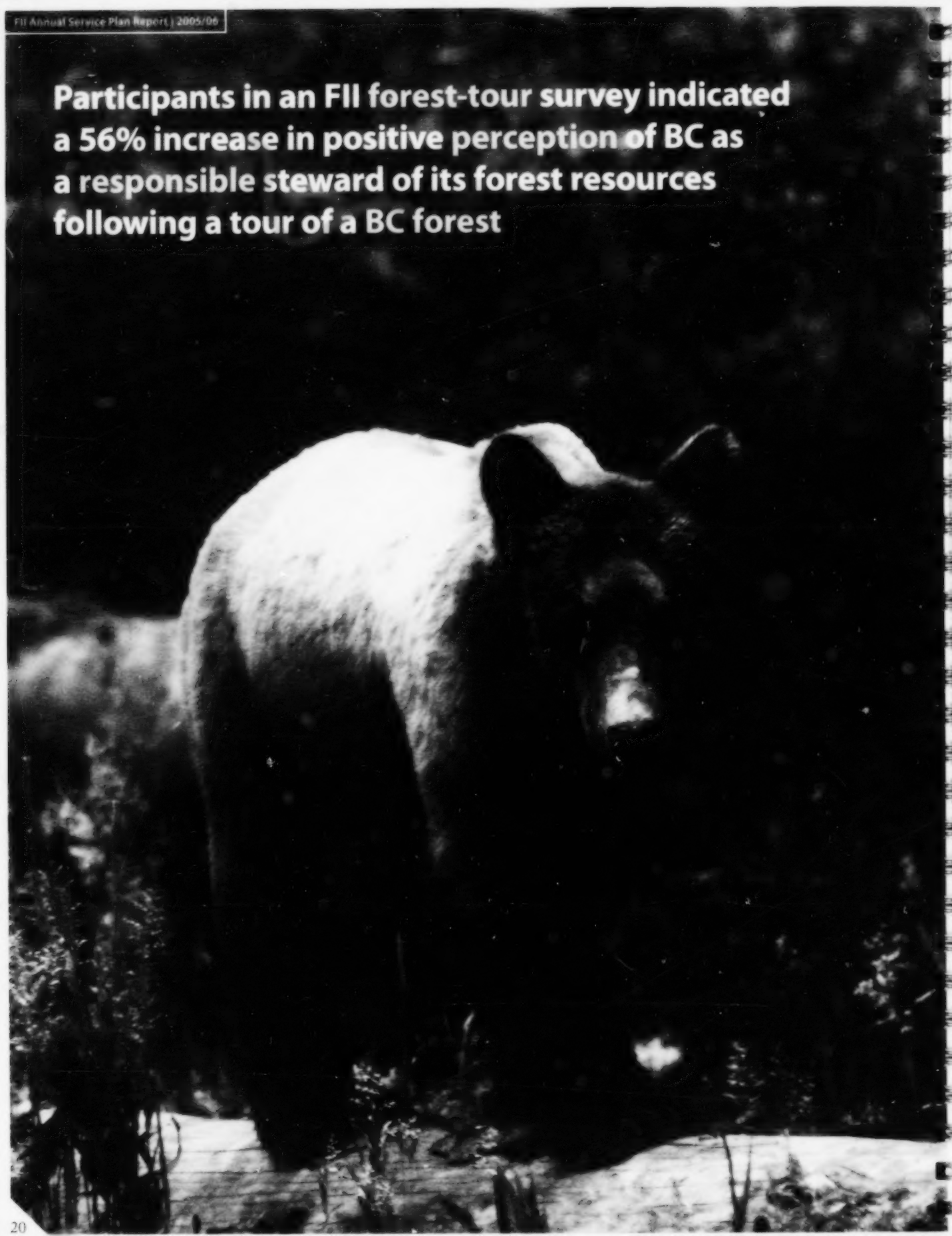
Results from the survey are being used to guide improvements to industry relations and communication.

### A results-focused organization

FII continued a strong record of investments, results and success in 2005/06. Investments in innovative market and product development as well as market-access projects are producing promising results including regulatory and building/fire code changes increasingly supporting the presence of BC wood in several Asian markets.

[1] These numbers represent a blend of percentage contributions in differing marketplaces.
[2] The Government of Canada, through the Canada Wood Export Program, invests 50% of project costs for projects outside of Canada and the United States.
[3] This number is a blend of the 15% and 45% shown in Table Goal 3 Objective 1.

**Participants in an FII forest-tour survey indicated a 56% increase in positive perception of BC as a responsible steward of its forest resources following a tour of a BC forest**



These results are the product of strong planning, on-the-ground advocacy and direct contact between FII partners and key government officials in the targeted markets.

As increasing attention focuses on the processing of and new uses for pine beetle wood, FII is investing in results-based projects to support the industry's use of this wood. Promising new information is coming from these trials and activities.

## An accountable and transparent organization

### Corporate Services

Throughout 2005/06, FII continued to deliver reports in accordance with its agreement with the Ministry of Forests and Range, including quarterly written reports and monthly financial reports. It also submitted its third service plan within the timeframes required in the Budget Transparency and Accountability Act.

### Financial management and control

During the year, FII completed an extensive review and made revisions to the previously existing financial policies and procedures manuals for both the Vancouver and China operations. This process was undertaken to continue to improve the financial control system that allows for the administration of funds in a fully accountable manner.

### Financial monitoring

Audits are underway for the recipient funding program for 2005/06 with June 30, 2006 set as the target date for completion of the audits. For the first time joint audits are being undertaken where programs were being funded jointly by both FII and CWEP (Canada Wood Export Program.) These joint audits are expected to reduce the overall cost of auditing for both FII, CWEP and funding recipients.

During the year internal audits were also completed on both the Vancouver and China operations. The results of these audits provided enough confidence to the audit committee that they approved a semi-annual audit program as opposed to the quarterly, and in the case of the China office, monthly audits in place at the beginning of the 05/06 fiscal year.

### Risk Management

FII continues to work on a risk management strategy for the Vancouver operation as well as FII Consulting (Shanghai) Co. Ltd. In March a Risk Identification Workshop was held with the FII executive to identify organizational risks within the FII group. A report identifying risks associated to the operations of FII has been completed and issued to the FII executive. The next step for the coming year will be to formulate a Risk Management Plan around the risks identified in this report.

### Human Resource Management

FII, with the approval of the Board of Directors, engaged a consultant to review FII's existing compensation plan, compare the compensation plan to the market, and if necessary provide recommendations to bring FII's compensation plan to competitive market rates for each employee position in the company. FII received approval of the consultant's recommendations from the Minister of Finance. Adjustments will be made through April 2007 to bring compensation to the approved level.

During the year, FII also appointed a director to manage the organization's new mountain pine beetle program. A satellite office was also established in Prince George to support the pine beetle management work in the heart of the affected region.

### Performance Management and Reporting

FII is in the process of creating an integrated performance management framework through direct linkages between desired program outcomes, specific market objectives and targets, and the individually funded projects (whether delivered by FII or by partners.)

Objectives and performance measures will be developed at five levels within FII.

**Strategic level** – the strategic plan establishes broad, long-term agency goals along with performance expectations (targets and performance measures.)

**Market level** – market strategies identify goals and performance expectations within specified markets.

**Service Plan level** – at the service plan level, broad goals and objectives for FII are established which support implementation of the strategic plan and market strategies.

**The program level** – at the program level, FII develops funding objectives which support implementation of the strategic plan, market strategies and the service plan. Performance measures are identified at the funding-objective level and relevant measures developed at the strategic, market and service plan levels are adopted when appropriate.

**The project level** – at the project level, funding recipients identify project objectives, along with relevant performance measures and targets that directly support funding objectives and market strategies.

FII views each of these levels as part of an integrated system that ensures that high-level performance expectations are reflected in operational activities.

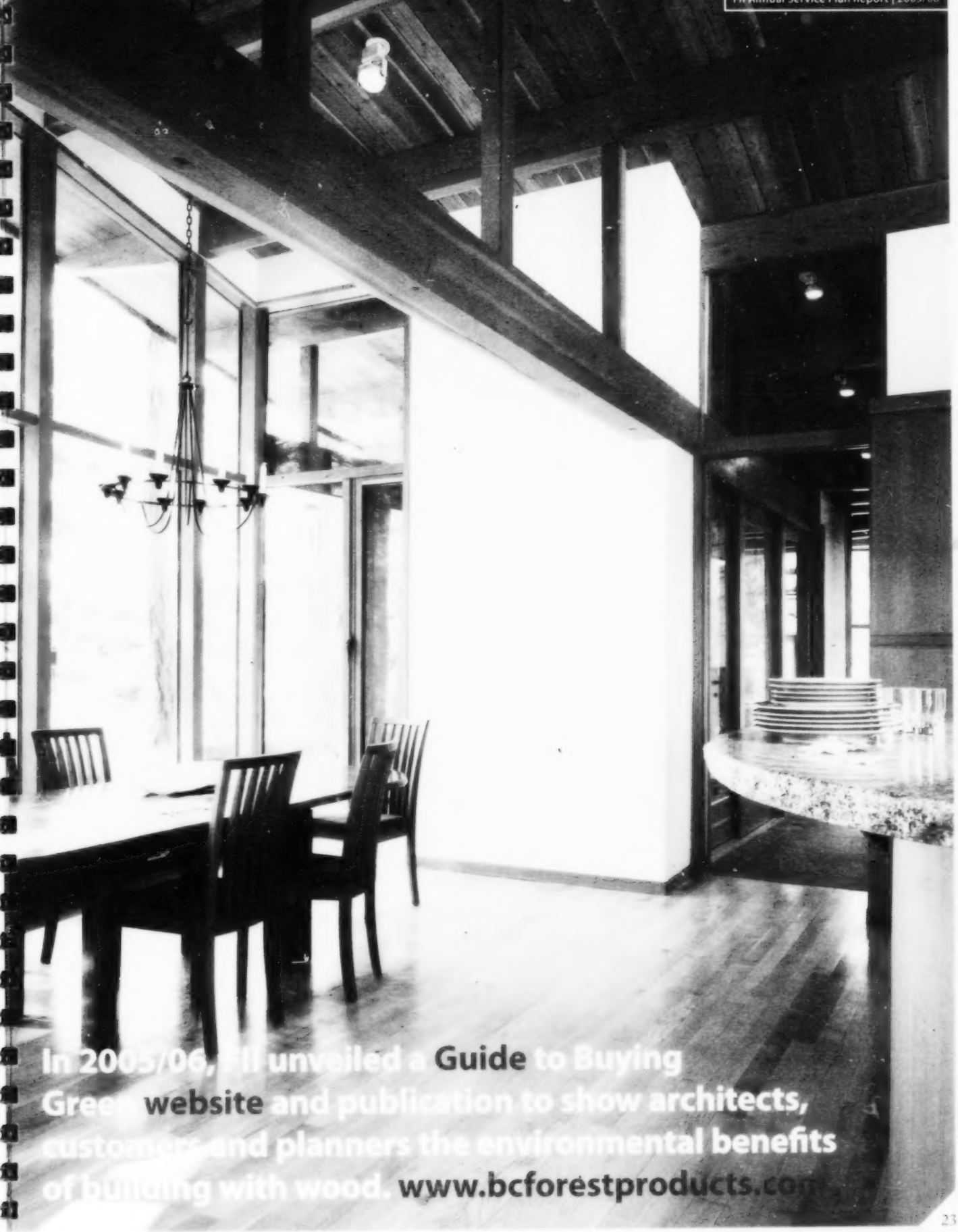
Accountability and responsibilities for performance monitoring and assessment exist at all levels within FII and extend to agencies which have been contracted to provide services or deliver initiatives on behalf of FII.

Roughly half of FII's annual investments are delivered by contracted partners, consisting of industry trade associations, forest research institutes, post secondary institutions, and other government ministries. While the responsibility for performance management rests with FII and its program staff, the accountability for investments and their successful contribution towards program and organizational goals is shared with each of FII's contracted delivery partners.

Forestry Innovation Investment's vision, mission and values, and the means by which they are put into practice, are fully consistent with the government's core values of integrity, fiscal responsibility, accountability, respect and choice.

Moreover, the successful discharge of FII's mandate contributes strongly to the province's economic strength.

| Government Strategic Plan | FII Alignment |
|---|---|
| To make BC the best educated, most literate jurisdiction on the continent. | A robust and successful forest industry is one of the largest contributors to the provincial economy and government revenues. Forest industry revenues to government are used to support education, health and other key BC priorities. By contributing to the strength of the forest industry, FII is contributing to the programs that support this government goal. (FII Goal 1) |
| To lead the world in sustainable environmental management, with the best air and water quality and the best fisheries management bar none. | FII will position BC as a world-leader in the sustainable management of the province's forest resource. (Goal 2) |
| To create more jobs per capita than anywhere else in Canada. | A well-performing forest industry is the economic backbone of the province. An estimated 90,000 people are directly employed in BC's forest industry. Working with partners in the public and private sectors, FII's goal is to help maintain and improve access to international markets for BC wood and product manufacturers. A strong forest industry will help ensure continued and growing employment for British Columbians. (Goal 1) |


In 2005/06, FII unveiled a Guide to Buying
Green website and publication to show architects,
customers and planners the environmental benefits
of building with wood. www.bcforestproducts.com

## GOAL 1: EFFECTIVE MARKETING OF BC FOREST PRODUCTS LEADING TOWARDS A ROBUST AND GLOBALLY COMPETITIVE FOREST INDUSTRY.

### OBJECTIVE 1: MAINTAIN OR IMPROVE ACCESS TO INTERNATIONAL MARKETS FOR BC WOOD PRODUCT MANUFACTURERS.

**Performance measures:**

Level of market access in target markets

| | | | |
|---|---|---|---|
| Inventory of market barriers and priorities identified. | Inventory completed and priorities identified in China, Korea, Japan, Europe and Australia. | The 2006/07 and 2007/08 targets have been changed to reflect the refinement of Goal 1 to: Diversified market opportunities for BC forest products. (see Appendix 1). | Review and update existing Japan strategy. |
| | | Update and expand Korea strategy. | Effective implementation of existing strategies. |
| Market access index implemented. | Market access index implemented for 06-07. | Effective implementation of existing strategies. | Demonstrated completion of milestone objectives in market access checklist. |
| | | Market access checklist implemented to quantify and track achievement of milestones in China and Korea. | Demonstration planning done in Korea. |
| Number of barriers removed to be determined. | **Removed target** Number of barriers not a priority in relation to the nature of the barriers. Priorities set based on market access index. | Develop United States non-residential strategy. | Implement US non-residential program. |
| | | Provide technical resources to promote wood use/ showcase wood in BC's Olympic facilities. | Designs for Olympic venues to incorporate BC wood products. |
| | | | Continued collaborative program of investments. |
| | | | Effective communication of the results of investments. |

### OBJECTIVE 2: POSITION BC AS A LEADER IN WOOD PRODUCT DEVELOPMENT, QUALITY AND MANUFACTURING EFFICIENCY.

**Performance measures:**

- Positive return on investment for FII-funded projects.
- Market opportunities for MPB wood.

| | | | |
|---|---|---|---|
| ROI realized by FII investments is at or higher than baseline: For every dollar invested by FII: | Third party analysis suggests that the economic benefits generated in year 2 will exceed $2 for every dollar invested. However, FII is allowing more time for program change implementation before further analysis. | With the 2006/07 Service Plan, Goal 1 has been refined and in turn, new targets created. (see Appendix 1) | With the 2006/07 Service Plan, Goal 1 has been refined and in turn, new targets created. (see Appendix 1) |
| $2 in economic benefits generated in year 1; $4 in economic benefits generated within the first three years of the investment. | | | |

## OBJECTIVE 2: POSITION BC AS A LEADER IN WOOD PRODUCT DEVELOPMENT, QUALITY AND MANUFACTURING EFFICIENCY.

**Performance measures:**

- Positive return on investment for FII-funded projects.
- Market opportunities for MPB wood.

| | | | |
|---|---|---|---|
| Analyze the qualities of MPB-affected wood. | Developed MPB market strategy, analyzed qualities of MPB-affected wood, and identified opportunities that address the changing fibre characteristics and new applications for MPB-affected wood. | Fund projects proposed by industry associations, Forintek and UBC. | Increased export opportunity for BC products made from wood affected by natural disturbance agents |
| Strategy for promoting the optimum use of MPB-affected wood. | 3 pilot projects carried out with prospective customers and market applications in China. | Self-initiate work to fill gaps identified by involved stakeholders. | Percentage target tbd. |

## OBJECTIVE 3: INCREASE MARKET ACCEPTANCE AND DEMAND FOR BC FOREST PRODUCTS IN EXISTING AND EMERGING MARKETS.

**Performance measures:**

Level of market/ customer acceptance for new/existing BC wood products.
Completion of the China demonstration project.

| | | | |
|---|---|---|---|
| Increase acceptance toward 80% customer acceptance level in 2005/06. | A late 2004/05 survey of customers indicated an average 70% acceptance of new and existing BC wood products. | With the 2006/07 Service Plan, Goal 1 has been refined and in turn, new targets created. (see Appendix 1) | With the 2006/07 Service Plan, Goal 1 has been refined and in turn, new targets created. (see Appendix 1) |
| 2nd phase completed (villas built and apartment renovation complete.) | Delays with regulatory approvals in China have pushed back the completion date into late 2006. | Implement new three-year China workplan.<br>Two villas completed in Shanghai.<br>One renovation project in Shanghai.<br>One demonstration project in Beijing.<br>China renovation market strategy in place. | One to two demonstration projects completed in China. |

## GOAL 2: BC IS POSITIONED AS A GLOBAL LEADER IN SUSTAINABLE FOREST MANAGEMENT.

**Performance measures:**

- Percentage of customers who perceive BC as a leader in sustainable forest management.
- Percentage of visitors to the BC forest information web site.
- Percentage of forest tour participants who view BC as a source of sustainable forest management.

| | | | |
|---|---|---|---|
| Maintain or increase the percentage of customers who perceive BC as a leader in SFM relative to the baseline. | The majority of customers surveyed in a 2005 survey perceived that forest practices in BC had improved. Some indicated this was due to increased communications around initiatives such as the collaborate process on the central coast. | Implement recommendations from 2005/06 survey of international customers. | Survey customers. |
| 5% increase in website visits during key information campaigns. | During the major central/ north coast information campaign, visits to the web site increased by 4.9%. | With the refinement of program goals and objectives this target has been removed. (see Appendix 1) | With the refinement of program goals and objectives this target has been removed. (see Appendix 1) |
| Percentage of forest-tour participants who view BC as a source of sustainable forest management. | The 2005/06 baseline survey of customers shows strong support for BC as a source of sustainable forest management. In a pre-tour customer survey, when asked if they considered Canada to be a responsible steward of its forest resources, 11% strongly agreed; 89% agreed.<br><br>Following the tour to BC, when asked the same question, 67% strongly agreed, and 33% agreed. Indicating a 56% increase in positive perception of forest management. | With the refinement of program goals and objectives this target has been removed. (see Appendix 1) | With the refinement of program goals and objectives this target has been removed. (see Appendix 1) |

## GOAL 3: A COORDINATED APPROACH TO MARKET DEVELOPMENT THAT OPTIMIZES PARTNER AND RECIPIENT CONTRIBUTIONS

### OBJECTIVE 1: INCREASED LEVEL OF PARTNER SUPPORT FOR FII-FUNDED PROJECTS AND INITIATIVES.

**Performance measures:**

- Leveraged funds as a percentage of total project costs.
- Percentage of industry partners satisfied or full satisfied with services provided by FII.

| | | | |
|---|---|---|---|
| Baseline for leveraging: 15% of total project costs paid by industry for international marketing projects in markets outside of North America. | Maintained baseline 15% of total project costs paid by industry. | A refinement of Goal 3 in the 2006/07 Service Plan (see Appendix 1) has resulted in the establishment of new targets: | A refinement of Goal 3 in the 2006/07 Service Plan (see appendix 1) has resulted in the establishment of new targets: |

## OBJECTIVE 1: INCREASED LEVEL OF PARTNER SUPPORT FOR FII-FUNDED PROJECTS AND INITIATIVES.

**Performance measures:**

- Leveraged funds as a percentage of total project costs.
- Percentage of industry partners satisfied or full satisfied with services provided by FII.

| | | | |
|---|---|---|---|
| 30% industry share for international marketing projects in the US. | Exceeded baseline. Average 45% of total project costs paid by industry. | In-market development activities with indicator of 50% contribution from industry and the federal government. | Continued partner investments in joint initiatives. |
| Maintain federal funding for FII-funded projects. | Federal funding maintained - 50% of total project costs paid by Government of Canada outside of Canada and the United States. | | |
| Baseline of industry satisfaction to be developed in 2005/06, through a survey to be conducted in the third quarter. | Formal survey completed. More than 9 in 10 people said FII has improved significantly in the past two years, with many citing greater collaboration and partnership on key issues. | Implement survey recommendations. | Survey partners on their views and support. |

## OBJECTIVE 2: INCREASED COORDINATION AMONG FOREST-SECTOR PARTNERS.

**Performance measures:**

- Value of projects funded through FII that support market strategies.
- Level of industry support for coordinated trade show strategy.
- Coordinated approach to the use of the Dream Home Canada facility.

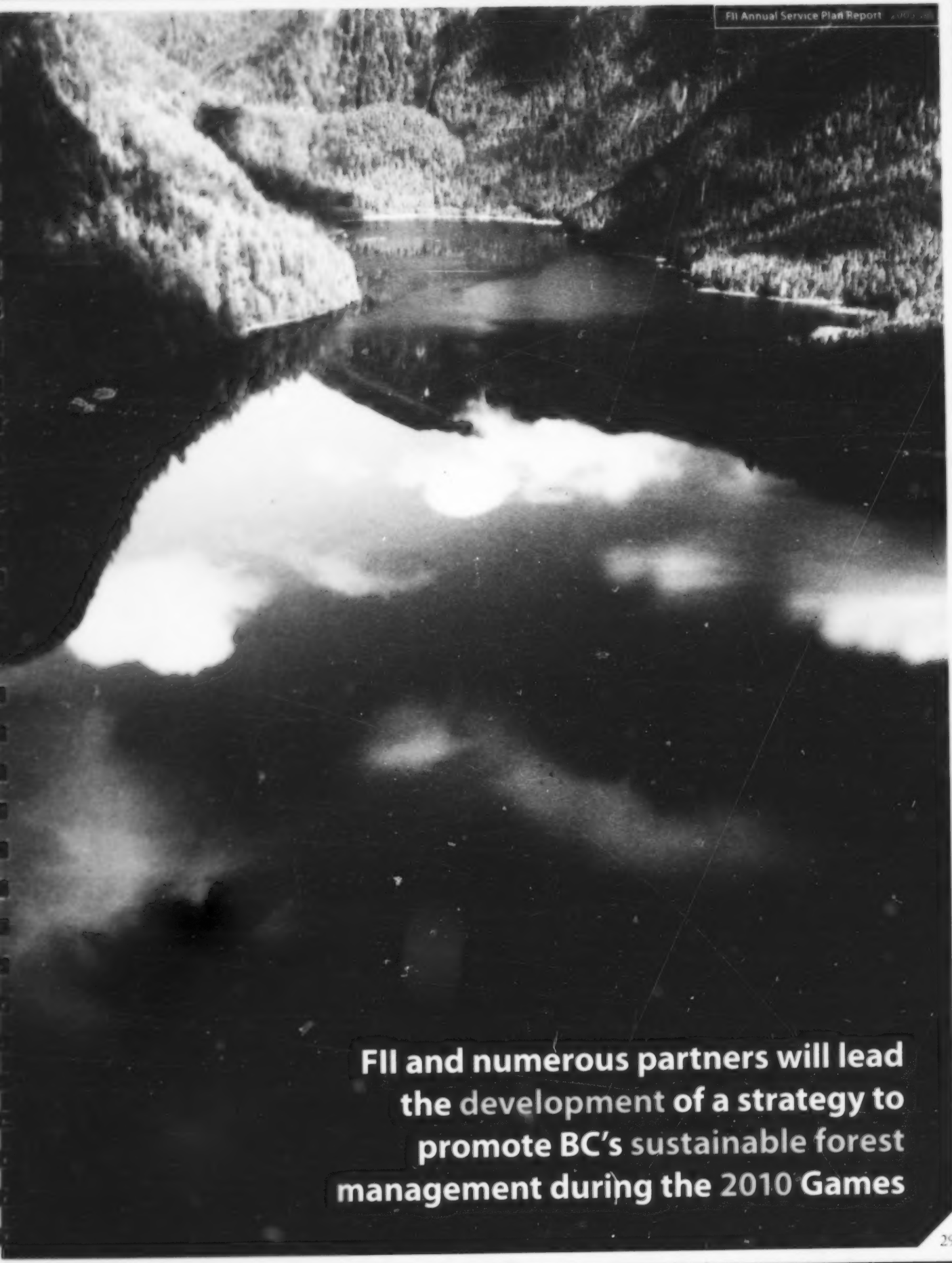
| | | | |
|---|---|---|---|
| Working with partners - establish market strategies:<br>• China<br>• Japan<br>• Korea<br>• Taiwan<br>• Europe | 100% of projects in Japan, Korea, Taiwan and Europe following relevant market strategies. | 100% of projects are in compliance with relevant market strategies. | 100% of projects are in compliance with relevant market strategies. |
| Coordinated China market strategy released and implementation beginning in 2006/07. | Strategy implemented through targeted activities under the Canada Wood Group umbrella. | Review of market strategies. | |
| Coordinated tradeshow strategy developed and implemented - 22 industry/ 5 association participants - Level of participation maintained or grown. | Maintained participation with 21 industry / 7 association participants. | Level of participation maintained or increased. | Level of participation maintained or increased. |
| Consolidate offices of FII and industry associations in Shanghai and develop 3-year plan for the use of the (DHC) facility and implement usage plan. | Offices consolidated, activities coordinated and three-year plan adopted for a more unified marketing and outreach approach to the China market. | | |

## GOAL 4: AN EFFECTIVE, WELL-MANAGED ORGANIZATION.

**Performance measures:**

- Comprehensive and meaningful policies and procedures that guide the conduct of individual employees and the organization.
- Compliance with policies and procedures.

| | | | |
|---|---|---|---|
| 100% of policies and procedures in place. | Target met. Policy and procedure development work complete. | A refinement of Goal 4 in the 2006/07 Service Plan (see Appendix 1) has resulted in the establishment of new targets: | A refinement of Goal 4 in the 2006/07 Service Plan (see Appendix 1) has resulted in the establishment of new targets: |
| Monthly China operations audits. | Strong complaince has allowed aduits to move to twice yearly. | Compliant internal and external financial audit reports. | Compliant internal and external financial audit reports. |
| | Staff satisfaction survey undertaken. | Implement recommendations from 2005/06 staff satisfaction survey. | Conduct new staff satisfaction survey. |



**FII and numerous partners will lead the development of a strategy to promote BC's sustainable forest management during the 2010 Games**

FII completed its third year of operations under an amended agreement between FII and the Province of BC as represented by the Ministry of Forests and Range. Prior to the fiscal year end, work was started on a "shareholders letter of expectations" which is becoming the standard working document for Crown Corporations. It is expected to replace the previous agreement between the Ministry of Forests and FII for the coming years.

During the year, FII received the full $22.8 million budgeted funding amount. FII's 2005/06 program costs were under-spent by $61,000 such that, in accordance with the agreement with the Province of BC, FII will be returning excess funds of $ 248,000 (which also includes $131,000 of earned interest and $56,000 of amortized contributed surplus) to the province.

During the year a commitment was made to the Vancouver Convention Centre Expansion Project to provide $4.0 million to showcase BC wood products in the public areas of the building. A total of $3.4 million has been advanced to the project to date.

FII Consulting (Shanghai) Ltd. is registered under the laws of the Peoples Republic of China and as such has a December 31st fiscal year end. As required under the laws of the Peoples Republic of China, an audit of FII Consulting (Shanghai) Ltd.'s December 31, 2005 financial statements was carried out. The financial statements of the parent company, Forestry Innovation Investment Ltd., include all of the transactions of the subsidiary during the parent company's fiscal year ended March 31, 2006.

Some funds were spent on capital transactions within the corporation including leasehold improvements and certain furniture, office and computer equipment. Payments for the construction of the Demonstration Centre (including the villas) at the Dream Home Canada site are included in the accumulated deferred revenue and capitalized pre-paid lease accounts. The completion of the Villas has been delayed due to regulatory issues but they are expected to completed in late 2006. Final accumulated costs of the Dream Home Canada project will be amortized over a three-year period starting in the fall when the villas are complete.

At year end, FII and its subsidiary had 18 full-time employees.

FII expects to continue being funded according to the terms of its agreement with the Ministry of Forests and Range. The Ministry has indicated that funding will amount to $27.52 million in 2006-07, which will include $2.25 million from its mountain pine beetle program. About half of the total will be pooled with funding from the Canada Wood Export Program and from trade associations, research institutes and universities to fund activities they will undertake in FII's Market Development programs. The other half will be used to fund activities initiated by FII.

Over the past three years, FII and its funding recipients have accumulated a great deal of market research information and technical product-related data. To some extent that material has been sitting on the shelf. In the coming year, FII will give a high priority to introducing a more pro-active extension program by which interested firms and individuals will be made aware of findings that should be useful to them. This will include new reports on market trends in all countries of interest to BC firms.

Because the mountain pine beetle epidemic is so significant, FII will deliver a dedicated program to explore new opportunities for timber killed by the epidemic. Initial priorities will be on solid-wood products but as timber quality deteriorates in the coming years, research and development will migrate into issues concerning the pulp and paper sector, and eventually into the realm of timber as a source of bio-energy.

FII will continue to promote the use of wood in non-residential applications. In the coming year it will focus on 2010 Olympics venues by funding the provision of technical expertise through the Canadian Wood Council, and by contributing directly to the iconic Richmond skating oval in support of a unique all-wood roof. FII will also contribute towards the use of BC wood products in the expanded Vancouver Convention Centre. In collaboration with Canadian members of the private-sector Wood Products Council, we expect to initiate promotion of wood in low-rise commercial, industrial, and institutional buildings in the United States.

FII's subsidiary in China will undertake the construction of two demonstration villas in Shanghai, a project that has been delayed for many months because of regulatory issues between the developer and the municipality. Having concluded an agreement at the end of 2005-06, we will demonstrate the merits of using wood trusses instead of light steel for re-roofing older apartment buildings in Shanghai. We expect to work with a developer to introduce BC wood products in other apartment renovation treatments and to build a demonstration hybrid apartment building, with lower floors of concrete and upper floors and roof made of wood.

FII completed its third year of operations under an amended agreement between FII and the Province of BC as represented by the Ministry of Forests and Range. Prior to the fiscal year end, work was started on a "shareholders letter of expectations" which is becoming the standard working document for Crown Corporations. It is expected to replace the previous agreement between the Ministry of Forests and FII for the coming years.

During the year, FII received the full $22.8 million budgeted funding amount. FII's 2005/06 program costs were under-spent by $61,000 such that, in accordance with the agreement with the Province of BC, FII will be returning excess funds of $ 248,000 (which also includes $131,000 of earned interest and $56,000 of amortized contributed surplus) to the province.

During the year a commitment was made to the Vancouver Convention Centre Expansion Project to provide $4.0 million to showcase BC wood products in the public areas of the building. A total of $3.4 million has been advanced to the project to date.

FII Consulting (Shanghai) Ltd. is registered under the laws of the Peoples Republic of China and as such has a December 31st fiscal year end. As required under the laws of the Peoples Republic of China, an audit of FII Consulting (Shanghai) Ltd.'s December 31, 2005 financial statements was carried out. The financial statements of the parent company, Forestry Innovation Investment Ltd., include all of the transactions of the subsidiary during the parent company's fiscal year ended March 31, 2006.

Some funds were spent on capital transactions within the corporation including leasehold improvements and certain furniture, office and computer equipment. Payments for the construction of the Demonstration Centre (including the villas) at the Dream Home Canada site are included in the accumulated deferred revenue and capitalized pre-paid lease accounts. The completion of the Villas has been delayed due to regulatory issues but they are expected to completed in late 2006. Final accumulated costs of the Dream Home Canada project will be amortized over a three-year period starting in the fall when the villas are complete.

At year end, FII and its subsidiary had 18 full-time employees.

FII expects to continue being funded according to the terms of its agreement with the Ministry of Forests and Range. The Ministry has indicated that funding will amount to $27.52 million in 2006-07, which will include $2.25 million from its mountain pine beetle program. About half of the total will be pooled with funding from the Canada Wood Export Program and from trade associations, research institutes and universities to fund activities they will undertake in FII's Market Development programs. The other half will be used to fund activities initiated by FII.

Over the past three years, FII and its funding recipients have accumulated a great deal of market research information and technical product-related data. To some extent that material has been sitting on the shelf. In the coming year, FII will give a high priority to introducing a more pro-active extension program by which interested firms and individuals will be made aware of findings that should be useful to them. This will include new reports on market trends in all countries of interest to BC firms.

Because the mountain pine beetle epidemic is so significant, FII will deliver a dedicated program to explore new opportunities for timber killed by the epidemic. Initial priorities will be on solid-wood products but as timber quality deteriorates in the coming years, research and development will migrate into issues concerning the pulp and paper sector, and eventually into the realm of timber as a source of bio-energy.

FII will continue to promote the use of wood in non-residential applications. In the coming year it will focus on 2010 Olympics venues by funding the provision of technical expertise through the Canadian Wood Council, and by contributing directly to the iconic Richmond skating oval in support of a unique all-wood roof. FII will also contribute towards the use of BC wood products in the expanded Vancouver Convention Centre. In collaboration with Canadian members of the private-sector Wood Products Council, we expect to initiate promotion of wood in low-rise commercial, industrial, and institutional buildings in the United States.

FII's subsidiary in China will undertake the construction of two demonstration villas in Shanghai, a project that has been delayed for many months because of regulatory issues between the developer and the municipality. Having concluded an agreement at the end of 2005-06, we will demonstrate the merits of using wood trusses instead of light steel for re-roofing older apartment buildings in Shanghai. We expect to work with a developer to introduce BC wood products in other apartment renovation treatments and to build a demonstration hybrid apartment building, with lower floors of concrete and upper floors and roof made of wood.

Also in China, we expect to take a lead role in creating an on-the-ground presence by the Program for Endorsement of Forest Certification schemes in order to ensure that future procurement policies in China do not unfairly discriminate against BC suppliers.

In Indonesia we expect to fund a training program to accompany the sale of pre-cut house components for tsunami-related reconstruction. The training program will be crafted and delivered by the BC Institute of Technology, with students drawn from builders, government officials, technical school faculty and aid agencies who are funding the reconstruction. FII hopes that this will open the door to wood-frame technology in Indonesia more broadly, and for using pre-cut components not only in disaster relief elsewhere in the world, but also for low-cost housing in many developing countries.

On behalf of the forest product sector more broadly in Asia, FII expects to be the prime source of provincial expertise in the work of the Asia Pacific Trade Council. In concert with the Ministry of Economic Development, FII may commission analyses to inform each Market Advisory Group's strategy development, and ultimately expects to assume much of the responsibility for delivering of those strategies in the years ahead.

FII staff will continue to work with trade associations to co-ordinate private-sector participation in a half-dozen key international trade shows. FII staff will participate in those events to promote BC wood products and make customers aware of the province's forest management record. Primarily during the summer months, FII will host in-coming tour groups composed of foreign customers and Canadian staff in US consulates, as well as groups brought together under the auspices of the federal/provincial International Forestry Partnerships Program.

In collaboration with numerous stakeholders, FII will lead development of a strategy for promoting BC's sustainable forest management during the 2010 Games. FII will provide significant support in communicating the success of land-use planning on the Central Coast and North Coast, and will undertake new research into the Green Building movement in the United States. It will also initiate a teaching kit for upper grades in the BC school system, based on the science and social impacts of the mountain pine beetle epidemic.

Finally, because collaboration with the federal government, the private sector, research institutions, and post-secondary schools is so fundamental to FII's corporate philosophy, we will continue to place our highest priority on active engagement with knowledgeable people in each of those constituencies, encouraging each to contribute its unique strengths in well defined and harmonized programs.

# Forestry Innovation Investment Ltd.

## Statement of Management Responsibility

Management, in accordance with Canadian generally accepted accounting principles, has prepared the financial statements of *Forestry Innovation Investment Ltd.* These statements present fairly the financial position of the Company as at March 31, 2006 and results of its operations and cash flows for the year ended March 31, 2006.

Management is responsible for the preparation, integrity and objectivity of the financial statements. Systems of internal control are developed and maintained by management to provide reasonable assurance that transactions are properly authorized, assets are safeguarded, and financial records are properly maintained to provide a reliable basis for preparation of the financial statements.

The Auditor General of British Columbia has performed an independent audit of the financial statements. The Report of the Auditor General outlines the scope of his work on the financial statements of *Forestry Innovation Investment Ltd.*

K. Baker

Ken Baker
Chief Executive Officer

Douglas Greig
Vice President, Finance and Administration

Vancouver, British Columbia
May 19, 2006

# Report of the Office of the Auditor General of British Columbia

*To the Members of the Board of Directors*
*of Forestry Innovation Investment Ltd., and*

*To the Minister of Forests,*
*Province of British Columbia*

We have audited the balance sheet of *Forestry Innovation Investment Ltd.* as at March 31, 2006 and the statements of operations and retained earnings, and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of *Forestry Innovation Investment Ltd.* as at March 31, 2006 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

*Victoria, British Columbia*
*May 19, 2006*

Errol S. Price, CA
Deputy Auditor General

| For the year ended March 31 | 2006 | 2005 |
|---|---|---|
| **Assets** | | |
| **Current assets** | | |
| Cash | **1,456** | 1,463 |
| Accounts receivable | **221** | 461 |
| Prepaid expenses | **349** | 496 |
| Program advances (note 4) | **466** | 349 |
| | **2,492** | 2,769 |
| **Dream Home China** (note 5) | **4,072** | 3,572 |
| **Capital assets** (Note 6) | **942** | 1,175 |
| | **7,506** | 7,516 |
| **Liabilities** | | |
| **Current liabilities** | | |
| Accounts payable (note 7) | **1,281** | 1,551 |
| Program payables (note 4) | **667** | 213 |
| Due to the Province of British Columbia (note 8) | **614** | 1,016 |
| | **2,562** | 2,780 |
| **Capital lease** | - | 4 |
| **Deferred revenue** (note 9) | **4,944** | 4,676 |
| | **4,944** | 4,680 |
| **Shareholders's equity** | | |
| Share capital (note 10) | - | - |
| Contributed surplus (note 11) | - | 56 |
| Retained earnings | - | - |
| | - | 56 |
| | **7,506** | 7,516 |

**Commitments (note 12)**

On Behalf of the Board

Chair - Doug Konkin

Director - Tamara Vrooman

The accompanying notes and supplementary schedule are an integral part of these financial statements.

| For the year ended March 31 | 2006 | 2005 |
|---|---|---|
| **Revenue** | | |
| Contribution from the Province of British Columbia | **22,050** | 16,454 |
| | **22,050** | 16,454 |
| **Program costs** | | |
| Market Development Programs | | |
| International Marketing | **10,576** | 6,755 |
| Product Development | **3,999** | 3,931 |
| China Market Development | **1,550** | 1,287 |
| Mountain Pine Beetle | **1,439** | - |
| **Total Market Development Programs** | **17,564** | 11,973 |
| **BC Market Outreach Network** | **2,496** | 2,736 |
| **Corporate Support** | **1,394** | 1,288 |
| **Amortization** | **652** | 547 |
| | **22,106** | 16,544 |
| **Excess of revenue over expenditures** | **(56)** | (90) |
| Transfer from Contributed Surplus (Note 11) | **56** | 90 |
| **Retained earnings end of the year** | - | - |

The accompanying notes and supplementary schedule are an integral part of these financial statements.

| For the year ended March 31 | 2006 | 2005 |
|---|---|---|
| **Cash flows used in operating activities:** | | |
| International Marketing | **(10,399)** | (6,794) |
| Product Development | **(3,817)** | (3,715) |
| China Market Development | **(1,290)** | (2,237) |
| Mountain Pine Beetle | **(1,446)** | - |
| BC Market Outreach Network | **(1,757)** | (1,592) |
| Corporate Support | **(1,415)** | (1,995) |
| Prepaid expenses | **(326)** | (456) |
| Final payments against previous March 31 accruals | **(2,191)** | (6,121) |
| | **(22,641)** | (22,910) |
| **Cash flows used in investing activities:** | | |
| Interest on investments | **127** | 45 |
| Asset acquisition | **(293)** | (782) |
| | **(166)** | (737) |
| **Cash flows from financing activities:** | | |
| Contribution from the Province of British Columbia | **22,800** | 18,750 |
| **Decrease in cash during the year** | **(7)** | (4,897) |
| Cash beginning of year | **1,463** | 6,360 |
| **Cash end of year** | **1,456** | 1,463 |

The accompanying notes and supplementary schedule are an integral part of these financial statements.

| | International Marketing | Product Development | China Market Development | Mountain Pine Beetle | BC Market Outreach Network | Administration | Amortization | 2006 Total | 2005 Total |
|---|---|---|---|---|---|---|---|---|---|
| **Amortization** | | | | | | | 652 | **652** | **547** |
| **Auditing** | 96 | 96 | | | | | | **192** | **280** |
| **Communications** | 47 | 9 | | | 8 | | | **64** | **-** |
| **Conferences and Trade Shows** | 985 | | | | 950 | | | **1,935** | **2,055** |
| **Development Costs** | 23 | 23 | | | | | | **46** | **-** |
| **Extraordinary Items** | | | | | | | | **-** | **421** |
| **Grants** | 4,175 | 10 | | | | | | **4,185** | **-** |
| **Marketing** | | | 256 | | | | | **256** | **-** |
| **Office** | 62 | 56 | 148 | 4 | 107 | 258 | | **635** | **563** |
| **Other** | 55 | | | | | | | **55** | **12** |
| **Performance Management** | 166 | 147 | | 10 | | | | **323** | **-** |
| **Professional Services** | 21 | 21 | 418 | | 15 | 277 | | **752** | **557** |
| **Publishing** | 211 | 9 | | | 126 | | | **346** | **337** |
| **Strategy & Research Studies** | 198 | 292 | | 12 | 541 | | | **1,043** | **1,652** |
| **Trade Missions** | | 322 | | | | | | **322** | **220** |
| **Travel** | 87 | | 42 | | 19 | 54 | | **202** | **146** |
| **Wages and Benefits** | 92 | 92 | 387 | 37 | 305 | 805 | | **1,718** | **1,362** |
| **Websites** | 18 | 4 | | | 19 | | | **41** | **2** |
| **Program Costs** | 4,340 | 2,918 | 299 | 1,376 | 406 | | | **9,339** | **8,390** |
| **Total** | **10,576** | **3,999** | **1,550** | **1,439** | **2,496** | **1,394** | **652** | **22,106** | **16,544** |

| | Current Year 12 months ended March 31, 2006 | Current Year Original Budget | Prior Year 12 months ended March 31, 2005 |
|---|---|---|---|
| **Funding** | | | |
| Receipts - Province of BC | $ 22,416 | $ 22,800 | $ 16,454 |
| Interest Income | - | - | - |
| Total Funding | $ 22,416 | $ 22,800 | $ 16,454 |
| **Expenditures** | | | |
| International Marketing | 10,854 | 9,365 | 6,755 |
| Product Development | 4,069 | 4,910 | 3,931 |
| China Market Development | 1,550 | 3,069 | 1,287 |
| Mountain Pine Beetle | 1,456 | 1,350 | - |
| BC Market Outreach Network | 2,496 | 2,840 | 2,736 |
| Corporate Support | 1,394 | 1,266 | 1,288 |
| Amortization | 652 | - | 547 |
| **Total Expenditures** | $ 22,471 | $ 22,800 | $ 16,544 |
| **Excess of Funding Over Expenditures** | $ (55) | $ - | $ (90) |
| Transfer from Contributed Surplus | 55 | | 90 |
| **Retained Earnings end of the year** | $ - | $ - | $ - |

## 1) Nature of business

Forestry Innovation Investment Ltd. (the Company), was incorporated on March 31, 2003 under the laws of British Columbia. A board of directors, all appointed by the government of British Columbia, governs the Company.

**Market Development Programs** - use project funding and partnerships with the Government of Canada, forest industry associations and research institutions, to:

- maintain and create opportunities for BC wood products in existing and emerging markets;
- ensure BC forest products have access to markets free from regulatory and other barriers;
- ensure buyers, consumers, designers, builders, developers and architects know about BC wood products and the many positive features they bring to wood-frame construction and interior finishing;
- support the development of innovative new forest products, including products using pine harvested from mountain pine beetle-attacked forests; and,
- provide markets and audiences with information on the properties and qualities of BC's premier forest products as well as the BC companies that supply them.

**BC Market Outreach Network Program** (BCMON) - is an in-house FII program that provides international buyers and others with credible facts that BC forest products come from well-managed forests.

Environmental campaigns that promote misleading or incorrect information are quickly challenged by BCMON staff and FII's partners. They also monitor the development of draft legislation and procurement policies that could impair the flow of BC forest products into a particular market, making relevant officials aware of unintended consequences if the legislation or policy is adopted.

The Company is exempt from federal and provincial income taxes.

## 2) Significant accounting policies

The financial statements have been prepared in accordance with Canadian generally accepted accounting principles. Significant accounting policies followed in the preparation of these financial statements are:

**a) Consolidation**

The Company incorporated a wholly owned subsidiary registered under the laws of the People's Republic of China – FII Consulting (Shanghai) Co. Ltd. The company was required so that business can be carried on in China. There are restrictions imposed on the distribution of earnings and other transactions with the foreign subsidiary and hence it has not been fully consolidated in these financial statements. However these financial statements reflect all the transactions of the subsidiary during the year.

**b) Construction in progress**

Costs incurred in the development and construction of the Dream Home China project have been deferred and will be amortized as lease payments over three years once the construction as been completed. Pre-development costs incurred prior to the approval of a project are expensed.

**c) Capital assets**

Capital assets are recorded at cost and amortization is being calculated on the straight-line basis using the following rates:

| | |
|---|---|
| Computer Equipment | 3 years |
| Computer Software | 2 years |
| Furniture and Equipment | 5 years |
| Leasehold Improvements | Term of Lease |
| Trade Show Booths | 3 years |
| Website development Costs | 2 years |

Assets costing less than $1,000 are expensed in the year of acquisition.

**d) Revenue recognition**

Contributions from the Province of British Columbia are for specific purposes and as such are deferred and recognized as revenue as the expenses are incurred.

**e) Foreign currency translation**

Any foreign currency transactions are translated into Canadian dollars at the rate of exchange in effect at the transaction date.

Any foreign currency denominated monetary assets and liabilities are stated using the prevailing rate of exchange at the balance sheet date.

**f) Use of estimates**

The preparation of financial statement in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts and disclosure of assets and liabilities at the date of the financial statements. Actual results could differ from these estimates.

## 3) Financial instruments

At March 31, 2006, the company's financial instruments include all cash, accounts receivable, other receivables, accounts payable and accrued liabilities. The fair values of the company's financial instruments approximate carrying amounts.

## 4) Program advances and payables

The company advances funds to recipient organizations during the year, based on recipient funding contracts, to carry out program activities. At March 31, 2006, $466,000 has been identified as repayable by the recipients and has been set up as program advances. Historically these unspent advances have been repaid back to FII prior to the end of the first quarter of the new fiscal year after fourth quarter reports have been submitted and final audits have been completed.

Program payables are set up in an amount of $667,000 and relate to the net amounts payable at March 31, 2006 for the programs being carried out in the subsidiary company FII Consulting (Shanghai) Co. Ltd.

## 5) Dream Home Canada

The Company provided the registered capital of $1,605,840 (US $1,200,000) to FII Consulting (Shanghai) Co. Ltd. through a grant agreement, whereby the funds are committed to the Dream Home China project and cannot otherwise be returned to the Company. The Company has entered into an agreement with a development company in China with respect to the construction and lease back of a demonstration centre and wood frame construction villas. All construction related costs of this project are being capitalized and will be expensed over a three-year period on the completion of the construction.

| | **2006** | 2005 |
|---|---|---|
| Registered capital | **1,606** | 1,606 |
| Construction-in-progress | **2,466** | 1,966 |
| | **4,072** | 3,572 |

**6) Capital Assets**

| | Cost | Accumulated Amortization | **2006 Net Book Value** | 2005 Net Book Value |
|---|---|---|---|---|
| Computer Equipment | 237 | 175 | **62** | 110 |
| Computer Software | 88 | 79 | **9** | 27 |
| Furniture and Equipment | 253 | 90 | **163** | 174 |
| Leasehold Improvements | 77 | 73 | **4** | 22 |
| Tradeshow Booths | 1,256 | 607 | **649** | 665 |
| Websites | 384 | 329 | **55** | 177 |
| | 2,295 | 1,353 | **942** | 1,175 |

Cost includes the fair market value of certain assets transferred to the Company from the Province effective April 1, 2003, for one dollar. The assets are reflected as contributed surplus.

**7) Accounts payable**

| | **2006** | 2005 |
|---|---|---|
| Trade payables | **346** | 1,491 |
| Accrued liabilities | **935** | 55 |
| Current portion of capital lease | **-** | 5 |
| | **1,281** | 1,551 |

**8) Due to the Province of British Columbia**

Increase in capital assets net of amortization represents capital assets acquired during the year of $419,170 less amortization on assets purchased by the Company $651,729 which is equal to $232,559.

| | **2006** | 2005 |
|---|---|---|
| Balance, beginning of the year | **1,016** | 1,169 |
| Funds received for current year operations | **22,800** | 18,750 |
| | **23,816** | 19,919 |
| Payments refunded back to the Province | **(1,016)** | (1,169) |
| Prior year program recoveries | **-** | 231 |
| Interest earned during the period | **132** | 45 |
| Program expenditures | **(22,050)** | (16,454) |
| Construction costs - Dream Home China Project | **(500)** | (1,228) |
| Decrease (Increase) in capital assets net of amortization | **232** | (328) |
| Due to the Province end of the year | **614** | 1,016 |

Decrease (Increase) in capital assets net of amortization represents capital assets acquired during the year of $419,170 (2005 $785,912) less amortization on assets purchased by the company of $651,729 (2005 $457,498) which is equal to $232,559 (2005 $328,414.)

### 9) Deferred revenue

The company defers contributions received from the Province of British Columbia and recognises revenue as expenses are incurred. The Deferred revenue account will increase by the purchase of assets and decrease by the amortization of those assets.

| | 2006 | 2005 |
|---|---|---|
| Balance, beginning of the year | **4,676** | 3,120 |
| Construction costs - Dream Home China Project | **500** | 1,228 |
| (Decrease)Increase in capital assets net of amortization | **(232)** | 328 |
| Balance, end of the year | **4,944** | 4,676 |

The Dream Home China Project estimated completion date is December 31, 2006 at which time the prepaid lease will begin to be amortized over a 3 year period.

### 10) Share capital

The Company has authorized capital of 100 common shares without par value of which 10 shares are issued and outstanding. The Minister of Forests and Range holds the shares issued as the designated representative of Her Majesty the Queen in right of the Province of British Columbia.

### 11) Contributed surplus

Contributed surplus represents the transfer of capital assets from the Province of British Columbia on the set up of the Company. This amount is being amortized each year equal to the amount of amortization taken on the capital assets.

| | 2006 | 2005 |
|---|---|---|
| Balance, beginning of the year | **56** | 146 |
| Amortization during the year | **(56)** | (90) |
| Balance, end of the year | **-** | 56 |

### 12) Commitments

The Company has lease commitments for the premises it occupies at 1130 West Pender and kiosk space at the Tsawwassen ferry terminal as follows:

| | Lease Amount |
|---|---|
| March 2007 | 121 |
| March 2008 | 96 |
| March 2009 | 20 |
| March 2010 | 20 |
| March 2011 | 4 |
| | 261 |

### 13) Related party transactions

The Company is related through common ownership to all Province of British Columbia ministries, agencies and crown corporations. Transactions with these entities, unless disclosed separately in these financial statements, are generally considered to be in the normal course of operations and are recorded at the exchange amount.

### 14) Comparative Figures

Certain figures for 2005 have been reclassified to make their presentation identical to that adopted in 2006.

The table below reflects changes to FII's goals and performance measures between the 2005/06 Service Plan Update (September 2005) and the 2006/07-2008/09 Service Plan (February 2006.)

Any new measures in the February 2006 Service Plan will be reported on in the next Annual Report.

FII has refined its goals and performance measures in response to changing market and industry conditions and to ensure our activities are easily understood by non-industry readers.

| Goals and Objectives 05/06 September Service Plan Update | | Goals and Objectives 06/07 February Service Plan Update | |
|---|---|---|---|
| Goal | Performance Measures | Goal | Performance Measures |
| **1. Increased demand for BC wood products** | Level of market access in target markets.<br><br>Positive return on investment for FII-funded projects.<br><br>Market opportunities for wood affected by mountain pine beetle. | **1. Increased demand for BC wood products** | Support the government's Asia Pacific Strategy by developing and implementing the forest sector strategies for each market.<br><br>Achievement of pre-identified milestones needed to enable access to new markets, such as new building and fire codes.<br><br>Implement demonstration projects to showcase BC wood products and wood-construction technology.<br><br>Implement a program to promote wood use in non-residential structures.<br><br>Implement the new Mountain Pine Beetle Program. |
| **2. BC is positioned as a global leader in sustainable forest management** | Percentage of customers who perceive BC as a leader in sustainable forest management.<br><br>Percentage of visitors to the BC forest information web site.<br><br>Percentage of forest-tour participants who view BC as a source of sustainable forest management. | **2. BC is positioned as a global leader in sustainable forest management** | Extent to which BC is seen as a reliable supplier of forest products from sustainably managed forests<br><br>BCMON's effectiveness at communicating and advocating for the BC forest sector. |

| Goals and Objectives 05/06 September Service Plan Update | | Goals and Objectives 06/07 February Service Plan Update | |
|---|---|---|---|
| Goal | Performance Measures | Goal | Performance Measures |
| **3. Coordinated approach to market development that optimizes partner and recipient contributions.** | Leverage funds as a percentage of total project costs.<br><br>Percentage of industry partners satisfied or fully satisfied with services provided by FII.<br><br>Value of projects funded through FII that support market strategies.<br><br>Level of industry support for co-ordinated tradeshow strategy.<br><br>Coordinated approach to use of the Dream Home Canada facility. | **3. Collaborative delivery of market-development activities that optimize provincial, federal and private-sector contributions.** | The demonstrated willingness of key partners to commit financial resources to joint initiatives.<br><br>Level of qualitative support for FII's collaborative efforts with partners. |
| **4. An effective and well-managed organization.** | Comprehensive and meaning-ful policies and procedures that guide the conduct of individual employees and the organization.<br><br>Compliance with policies and procedures. | **4. An effective and well-managed organization.** | Funding recipient and FII staff compliance with comprehensive and robust policy and planning framework.<br><br>Degree of staff commitment to the organization. |

**BCMON** The BC Market Outreach Network, an in-house FII program.

**COFI** The Council of Forest Industries, a BC forest industry association representing BC forest companies.

**CWEP** Canada Wood Export Program, a program operated by National Resources Canada, a Government of Canada department.

**DHC** Dream Home Canada – The name given to FII's Shanghai demonstration centre and the multi-year initiative to introduce wood-frame construction and increased BC forest products to China.

**FII** Forestry Innovation Investment Ltd.

**IBS** International Builders Show.

**IMPD** International Marketing and Product Development – the name of two FII business areas prior to their realignment under the newly named Market Development Business Area.

**LEED** Leadership in Energy and Environmental Design.

**MDBA** Market Development Business Area – A group of programs operated by FII.

**MDF** Medium density fibreboard is a panel product used extensively in construction.

**OSB** Oriented strand board is a panel product used extensively in construction.

**ROI** Return on investment is a comparison of the money earned (or lost) on an investment compared to the amount of money invested.

**SPF** Group A group of companies manufacturing spruce, pine and fir (SPF) wood products.

**Contact us**

For more information on Forestry Innovation Investment Ltd. and its programs, please contact us at:

**Forestry Innovation Investment Ltd.**

Suite 1200, 1130 West Pender Street,
Vancouver, British Columbia
V6E 4A4 Canada

**Telephone:** 604-685-7507
**Fax:** 604-685-5373
**Email:** info@bcfii.ca
**Web site:** http://www.bcfii.ca

Forestry Innovation Investment Ltd.

BRITISH COLUMBIA
The Best Place on Earth